



RESEARCH REPORT

Catalytic Capital for Neighborhood Reinvestment

Lessons from Cleveland

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Catalytic Capital for Neighborhood Reinvestment

Catalytic capital is flexible money in search of social good. It is delivered through different financial instruments—including debt, credit enhancements, and equity. Regardless of the financial instrument used, catalytic capital fills gaps in funding from the mainstream private market. Catalytic capital investments often require accepting lower returns, higher risk, smaller deal sizes, and more patient terms. Catalytic capital investors may be the first investors in a deal, making predevelopment investments to help sponsors prepare their projects to receive other capital.

In the US, catalytic capital investing means targeting projects that have the potential to benefit people and places historically denied access to capital in ways that will help them thrive (Theodos et al. 2021). Catalytic capital investors seeking to support thriving neighborhoods often focus their investments on projects such as affordable and mixed-income housing, microbusinesses, community facilities like schools and health clinics, commercial real estate developments that create jobs and/or provide neighborhood services and shopping, and other projects that create economic and social benefits for communities, such as clean energy. These efforts can focus on both place-based outcomes (such as increasing homeownership rates or decreasing abandonment in a neighborhood) and people-based outcomes (such as improving health or access to quality jobs).

This brief seeks to explain how catalytic capital works by looking at models of its successful deployment and limitations to the benefits it can generate. We use the city of Cleveland, Ohio—a place with a deep history of catalytic capital investing for neighborhood revitalization—to illustrate and explore broader themes that we think are applicable to impact investors, community developers, philanthropies, and governments. Before beginning this exploration, we clarify how we are focusing our study of catalytic capital for the purposes of this brief:

- We focus on nongovernmental catalytic capital investors, including traditional and community foundations, high-net-worth individuals and other philanthropists, corporations making mission-driven investments, anchor institutions, community development financial institutions (CDFIs) and other nonprofit lenders and investors, and quasi-public entities making loans or investments. We choose this focus in part because a major goal of the Catalytic Capital Consortium that funded this research is enticing more nongovernmental players to make catalytic capital investments. That said, governmental players have played important roles working alongside nongovernmental catalytic capital investors to revitalize neighborhoods,

and we will note here that many nongovernmental investors are themselves bolstered by government programs.

- We focus on catalytic capital investments and not on other forms of catalytic support, such as standalone grants and operating supports. For example, we focus on loans to small businesses, but not grants to small-business training programs. We make this analytic choice because of the interest underlying this research in encouraging nongovernmental actors to include catalytic capital as a part of their investment portfolio. That said, it is clear from our research that catalytic capital providers and their partners use grantmaking to pave the way for future catalytic investments.
- For quantitative analysis, we proxy for catalytic capital investing by quantifying loans made by mission-driven entities such as CDFIs, foundations, religious institutions, and quasi-public institutions. Our data on mission lending is incomplete, due to limitations in the underlying data sources that we can access. However, we do think the proxy is still useful for our main objective in illustrating how catalytic capital investing works in place.

Catalytic Capital and Neighborhood Investment Flows—the Cleveland Context

Neighborhoods need capital to prosper, as capital allows people to buy homes, open businesses, build schools, and develop real estate projects. Yet a combination of factors can cause neighborhoods to be starved for investment, including racial discrimination, biases in property valuation, wealth gaps, and low investor confidence in neighborhood health (Rothwell and Perry 2022).¹ Our prior research has documented significant disparities in capital flows to metropolitan neighborhoods based on their racial makeup and poverty level (Theodos and Hangen 2019).² Rural areas are also disadvantaged in investment flows relative to urban areas (Theodos, González-Hermoso, and Hariharan 2021). A key objective of catalytic capital investment for neighborhood development is to counteract these forces and open up underinvested places and people so that mainstream capital will flow.

In Cleveland, neighborhoods have experienced severe disinvestment, concomitant to a decades-long citywide decline in population and jobs. Some of this citywide trend could be blamed on regional economic stagnation, but population and job losses in Cleveland account for all of the decline in Cuyahoga County. Mainstream capital flows in Cleveland for small business loans, commercial real estate investment, and home mortgages are much smaller than for many other US cities, even after adjusting for the base of population, jobs, and homeowners in each city. Consonant with our research in other cities, we also see significant race- and poverty-based disparities in neighborhood investment flows in Cleveland. For example, majority-White neighborhoods in the city have received over two

times the average aggregate capital flows per household of majority-Black neighborhoods (Theodos et al. 2023).

Community developers in Cleveland have thus been faced with the challenge of jump-starting a new process of growth and investment across the city, while simultaneously seeking more equitable outcomes for neighborhoods of color and lower-income neighborhoods that have experienced the greatest investment disparities. This challenge is fundamentally different from the problems that “hot market” cities like Seattle or Boston experience, where social equity concerns are tackled within a context of strong citywide capital investment, high real estate valuations, and the ever-present risk of displacement. For this reason, catalytic capital in Cleveland has often flowed to market-rate real estate projects intended to rebuild and repopulate neighborhoods, a role it would be unlikely to play in cities that are rapidly growing.

Who Invests Catalytic Capital in Neighborhoods?

We find catalytic capital investors make catalytic capital investments either because the social good they create is an explicit part of their organizational mission or because they have a strong attachment to a particular place, as is the case for anchor institutions, some corporate investors, and some individual investors.

In our Cleveland research, we compiled data on lending by mission-driven actors, by scanning datasets of commercial real estate transactions and by merging various data sources on CDFI lending activity. We also conducted both desk research and interviews to learn about catalytic capital investment activity around the city. Catalytic neighborhood investment in Cleveland appears to be driven by three major categories of nongovernmental actors, who often work in close collaboration with one another. We discuss their roles and some associated limitations for each below.

Local Philanthropy

As one interviewee noted, Cleveland has “a wealthy philanthropic community, and there are organizations with large local funds that use their money to do catalytic investing—like PRIs [program-related investments].” Leading foundations include the Cleveland Foundation—the second-largest community foundation in the US, with assets of \$3.2 billion; the Gund Foundation; and large private foundations such as the Mandel Foundation. Another interviewee observed that the philanthropic sector has worked to coordinate its investing activities. One observer reflected, “the big foundations

communicate, let each other know what they are working on. There seems to be this synergy—a follow-the-leader-thing at times—for big investments: they will do it together or they will avoid it.”

Foundations in Cleveland have made direct, project-level investments and investments in other catalytic capital providers such as CDFIs.

The most common way that philanthropies deliver catalytic capital is through program-related investments (PRIs). PRIs are highly flexible instruments that can deliver capital at below-market terms in exchange for impact. It can be harder for philanthropies to deliver catalytic capital that is structured as mission-related investments (MRIs). MRIs are investments out of the corpus of a foundation’s investment portfolio. Because of regulatory requirements that such investments be made on “prudent” terms, these investments are often not made on concessionary terms, which makes achieving impact goals more difficult (Tomasko et al. 2023). One observer related that foundations have sought to structure MRI investments at rates of return “as high or higher than bank capital,” and have also sought to position these investments in a senior spot in the capital stack relative to CDFI investments. This challenge stems in part from regulatory concerns over whether foundations are violating their fiduciary duties if they do not seek to maximize the prudent management of their endowments.³

BOX 1

Case Study: Building the Catalytic Capital Investing Practice at the Gund Foundation

Established in 1952, the George Gund Foundation (Gund Foundation) has been a leader in catalytic capital investing in Cleveland. It made its first program-related investments (PRIs) in the mid-1980s, and has since provided over \$20 million in PRIs, focused on sustainable neighborhood development and cultural assets in Cleveland. Five key themes emerge.

Working in partnership with other funders. A key to the Gund Foundation’s involvement in catalytic capital investing has been its longstanding partnership with the Cleveland Foundation. The foundations have invested together at the project level in, for example, the Lexington Village housing development in the Hough neighborhood and the Uptown project in University Circle. They have also invested together in intermediaries such as Village Capital Corporation. They emphasized an “invest together” theme, enabling each participating foundation to expand their impact, share insights, and mitigate concentrations of risk. As one interviewee shared, “It absolutely has helped both foundations deploy more catalytic capital than they would have alone.”

Establishing expectations and shared norms. The foundations have worked to establish shared expectations and norms around how nonprofits, other foundations, and private capital providers work together. The Gund Foundation worked to create a Cleveland-region marketplace with well understood rules about how the private sector and philanthropic community would work together, how deals were analyzed and underwritten, how to arrive at terms on details such as repayment priority and collateral

requirements, and how to work together in forbearance or unwinding on the rare occasion when deals didn't meet original expectations.

Supporting local intermediaries to boost community development ecosystem capacity. The Gund Foundation (with Cleveland Foundation and others) used operating grants to build the capacity of community development groups in which it later invested. For example, decades ago it provided operating and project grants that helped form the Detroit Shoreway Community Development Corporation. Once this corporation was established, it put together development deals in which catalytic capital providers invested. The foundations soon realized there was a missing piece to the ecosystem, however. As an interviewee shared, “the foundations provided grant funding to a lot of grassroots groups, yet soon realized ... structures were needed to increase the borrowing capacity and standing of these grassroots organizations.” Both the Cleveland and Gund Foundations invested in Cleveland Neighborhood Progress, Inc., a citywide community development intermediary that provides capacity-building and grantmaking for community development corporations (CDCs), and helps with equitable neighborhood planning, land assembly and development work, local data analysis and policy advocacy, and access to capital. Both foundations also invested in the Cleveland Housing Network, which has worked as a codeveloper creating capacity to do housing rehabilitation and new housing development around the city.

Using a variety of investment structures. PRI loans have long been a mainstay of the Gund Foundation's catalytic capital investing, since they are exempt from IRS requirements that forbid “jeopardizing investments,”⁴ so long as they advance their charitable mission first and consider financial return second. However, the foundation has used other forms of investment as well, including cash deposits with community-based lenders, equity investments, and mission-related investments (MRIs) out of the foundation's investment corpus. More recently, the Foundation's board, investment committee, and staff embarked on an exhaustive process to learn about approaches to invest the whole of the portfolio in ways that align with the same values with which they approach their grant and PRI making. The expansion into MRI investing was a more recent culture shift for the Foundation. As an interviewee shared, “Now the Gund Foundation considers both financial ROI and metrics for social and environmental impact in its selection and evaluation of fund managers on performance.”

Maintaining flexibility after the deal is made. At multiple points, the Gund Foundation has had to exercise patience and flexibility so that its PRI investments could achieve their mission and financial goals. For example, the Gund Foundation converted portions of several loans to Village Capital Corporation to recoverable grants to create more equity on a CDFI's balance sheet, enabling it to leverage more outside investment. During the Great Recession, the foundation renegotiated terms on many loans in its portfolio, adjusting interest rates, lengthening repayment periods, and converting balloon payments to more traditional amortization schedules. The foundation also performed a stress test on the PRIs in its portfolio at the outset of the COVID-19 pandemic and provided repayment forbearances on some deals, for example, to the Uptown project in University Circle.

CDFIs

Cleveland is home to a number of strong local CDFIs, including Village Capital, CHN Housing Capital, Jumpstart, and Cleveland Development Advisors. It also benefits from the presence of national-scale CDFI loan funds, such as Enterprise Community Partners and Local Initiatives Support Corporation (LISC). Collectively, these CDFIs cover a range of lending and project types including small business, venture capital, commercial real estate, and housing. GrowthOpps, a small business lending CDFI, has also emerged as a green bank making clean-energy-related investments in the city.

CDFIs obtain their capital from a variety of sources, including federal, state and local government sources (most notably the US Department of Treasury's CDFI Fund), foundations, and banks motivated by Community Reinvestment Act (CRA) concerns. Recently, some national CDFIs—including both LISC and Enterprise—have also had success raising investments from corporate impact investors, including through bond issuances.

CDFIs sometimes struggle to obtain capital on the terms that they need to make catalytic capital investments. CDFIs' capital providers may demand short terms or market returns, or impose stringent underwriting requirements or financial covenants that limit CDFIs' abilities to use the funds in relatively low-return, high-risk, and, ultimately, high-benefit ways. For example, a CDFI representative we interviewed mentioned a program for which the lender, in partnership with a regional bank, began to invest in entrepreneurs of color. Some of the bank's money in the program was a gift from its philanthropic arm, but the bulk was an investment by the CDFI. "The investment was structured to be a little more flexible than mainstream," the CDFI executive noted, "but I am not sure the bank really understands how flexible it needed to be."

BOX 2

An Example of How a CDFI Plays a Role as a Catalytic Capital Provider: Village Capital Corporation

Village Capital Corporation, a CDFI loan fund, was founded in 1992 as an affiliate of Cleveland Neighborhood Progress, a citywide community development intermediary. It finances both market-rate and affordable residential, commercial, retail, industrial, and mixed-use projects. Since its inception, it has provided nearly \$100 million in loans to support almost \$1 billion in total development costs for over 200 projects; helping to create and preserve over 8,100 residential units and more than 2 million square feet of commercial space.⁵

Village Capital does not have the scale of large national CDFIs, but its local focus enables it to play a significant role in the Cleveland community development ecosystem. Village Capital understands Cleveland's neighborhood markets, knows the partners who can help developers at the city, county and

state level, and is committed to the long-term success of local developers even when that requires concessions as a lender. Neighborhood Progress (Village Capital's parent corporation) has moved its offices around the city over the years—from Detroit Shoreway to Ohio City and now to the St Luke's campus in Buckeye-Shaker - and has used that presence to inform investments in the surrounding neighborhoods. Village Capital's local knowledge has enabled it to make small loans as well as large loans—for example, it provided a \$25,000 loan to a homeless shelter in Buckeye for building repairs, a deal that would be very difficult for an out-of-state lender to underwrite.

Village Capital has played a significant role in the revitalization of many Cleveland neighborhoods. For example, in Ohio City, Village capital invested in a sizable number of deals around its relocated headquarters. These investments included loans to the development affiliate of Cleveland Neighborhood progress as well as loans to for-profit developers for subordinate debt on three apartment buildings. When the Great Recession hit, Village Capital made loan modifications on those deals, but was ultimately repaid in full. Says Village Capital's current President, Dione Alexander, "We did all of the development on West 25th Street and around the West Side Market when it was not a nice place. Now people look at it as a model neighborhood—there have been 800 units developed over the past 24 months." Another of the investments Village Capital made in Ohio City was in a Dave's Supermarket—the second store out of 14 in what is the only supermarket chain in Cleveland. Since then, says Alexander, "we've financed every Dave's in the city at concessionary pricing." Later in the report we detail catalytic investments made by Village Capital in the University Circle, Detroit Shoreway, and Midtown neighborhoods—all places where significant neighborhood investment has been catalyzed.

Both grant equity and below-market, long-term debt from foundations, including the Gund and Cleveland Foundations, have played a key role in capitalizing Village Capital, alongside CRA-motivated bank debt from players such as US Bank and Charter One (now Citizens). The foundations invested in the CDFI to create a vehicle that would allow retail deals to happen that were too small and time consuming for the foundation staffs to properly vet and document individually. Debt-to-grant-equity conversions by foundations, including a \$1.5 million conversion by Cleveland Foundation, played a key role in helping the CDFI survive the Great Recession. Staff believe that continued support from catalytic capital providers will be critical to the organization's mission, particularly as a significant debt investment made by the Cleveland Foundation and extended to a 30-year term in 2002 begins to approach its horizon.

Anchor Institutions

Anchor institutions such as hospitals and universities have been widely credited in Cleveland for investing their resources to make projects happen. A major report published by the Cleveland Foundation documents how 19 anchor institutions in the University Circle neighborhood, including Case Western Reserve University and the University Hospital System, coordinated their investment

activity over a period of many years to radically transform the neighborhood (Cleveland Foundation 2013). The Cleveland Foundation played a convening and coordinating role to quarterback the initiative, which relied on the participation of both community-based nonprofit development entities and for-profit developers.

As might be expected, anchor institutions in Cleveland have principally invested in projects with a direct bearing on their business (such as new dormitories for a university or new medical facilities for a hospital). And they have typically had a place-based focus directly around their institutions. Much of the impact anchor institutions have had on Cleveland neighborhoods comes from their own institutional expansion, for example in University Circle and Midtown. Also, much of their catalytic impact has not been achieved through capital investment, but by using institutional purchasing power to support the creation of local, worker-owned cooperatives providing services such as laundry and energy services, and by creating programs to encourage institutional employees to live locally. That said, anchor institutions have played a role directly and indirectly providing and facilitating investment.⁶ Anchor institutions have also supported predevelopment activities via grant funding from a number of University Circle institutions for planning efforts and studies to support transit investments.

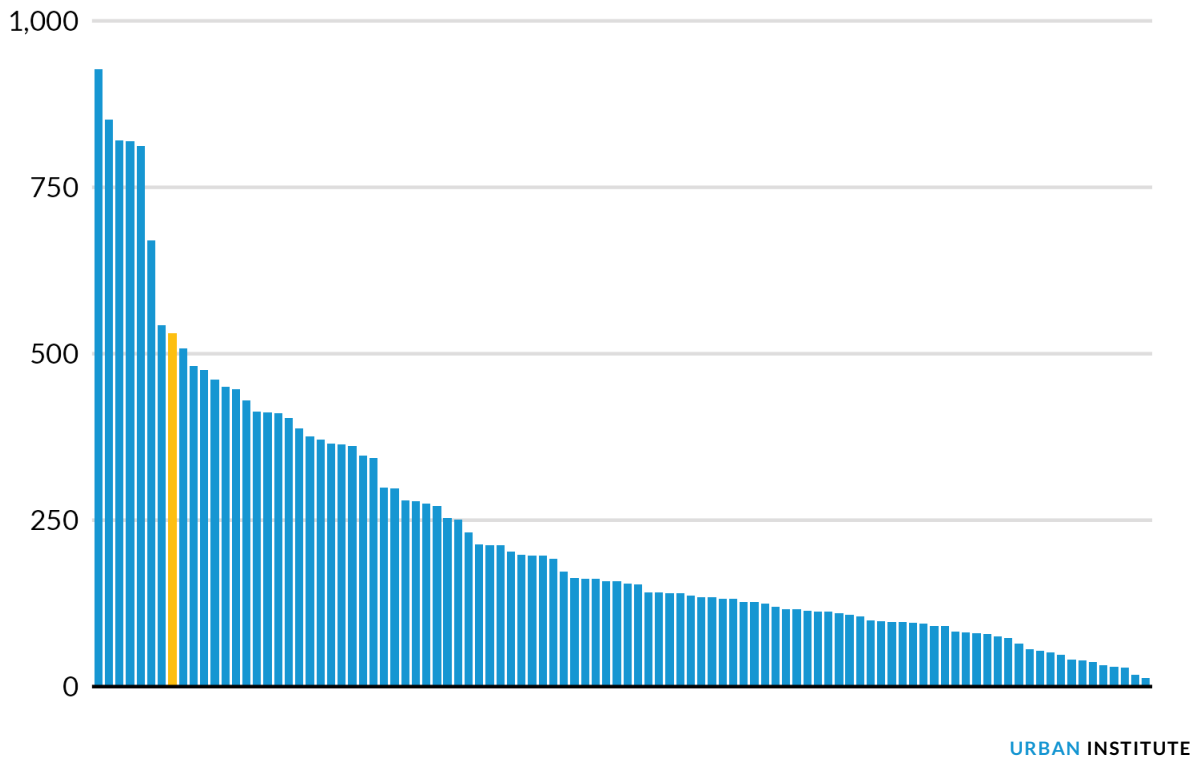
In Cleveland, as in many other cities, many anchor institutions are nonprofit entities exempt from property tax, which can be a point of contention in a city with limited resources. One stakeholder we spoke with noted that “much of the good work [of anchor institutions] is payment in lieu of taxes.”

How Much and Where Does Catalytic Capital Flow?

Cleveland has one of the highest rates of mission lending in the country on a per-household basis, which is how we measure catalytic capital investing activity. With over \$1 billion of this lending over the past 15 years, or a little over \$500 per household, Cleveland ranks eighth among the 100 largest cities in mission investment (figure 1). This total likely understates the actual level of mission lending, as available data are incomplete and many catalytic investments are not structured as mortgages that would appear in public records or in proprietary lending data from data vendors.

FIGURE 1

Mission Investment per Household for Cleveland, Ranked with the 100 Largest Cities
Between 2010 and 2020



Sources: US Census Bureau 2012–2020 five-year American Community Survey data; City of Cleveland, administrative data; CDFI Fund 2010–2020 Transaction Level Report; CoreLogic 2010–2020 mortgage data; US Department of the Treasury 2010–2020 New Market Tax Credits data; and Opportunity Finance Network 2010–2017 transaction data.

Catalytic capital in our data amounts to roughly 5 percent of lending in Cleveland. This is impressive, considering that catalytic capital is less than 1 percent of all lending in the US. This illustrates, however, that even in a market like Cleveland, mainstream capital flows are far larger than mission capital flows. As a result, catalytic capital in and of itself cannot counterbalance disparities and deficits in the provision of mainstream capital. This is why catalytic capital investors must be judicious and highly strategic about how they deploy their limited resources.

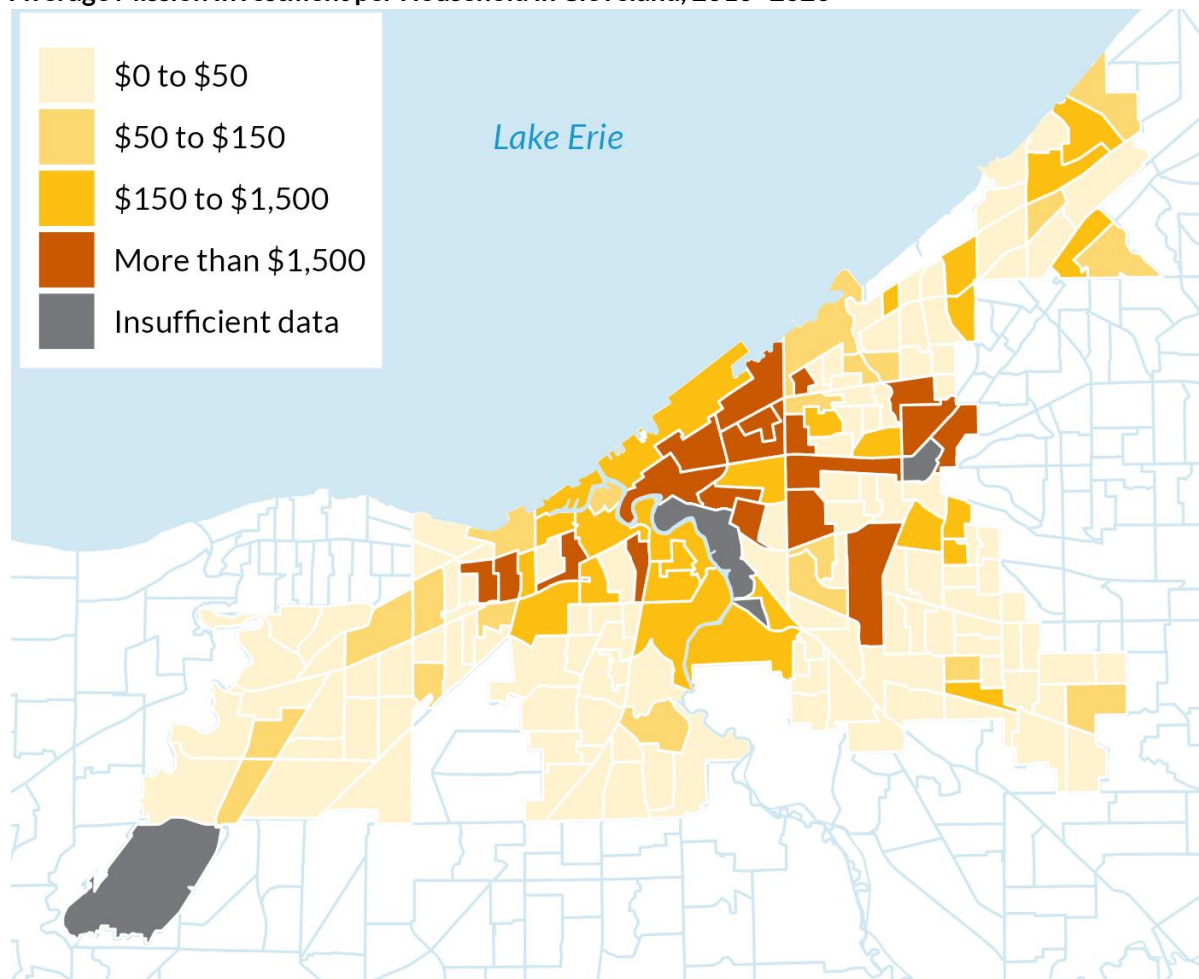
As shown in figure 2, most neighborhoods in Cleveland have seen mission lending activity over the past decade. This may reflect the reality that on a citywide basis, Cleveland is still working to rebuild its population and economic base, a task that requires the involvement of catalytic capital lenders in many neighborhoods.

However, through neighborhood tours and interviews, the research team observed that catalytic investment has not been equal across Cleveland neighborhoods. Some neighborhoods have seen

sustained and planned investment to drive their revitalization, and others have not. Achieving equitable development outcomes has long been a policy priority in Cleveland. At the same time, many catalytic capital investors have strategically focused on and built out from areas with strong market potential, rather than focusing their efforts on the weakest-market neighborhoods or attempting to evenly seed all neighborhoods with investment.

FIGURE 2

Average Mission Investment per Household in Cleveland, 2010–2020



Sources: US Census Bureau 2012–2020 five-year American Community Survey data; City of Cleveland, administrative data; CDFI Fund 2010–2020 Transaction Level Report; CoreLogic 2010–2020 mortgage data; US Department of the Treasury 2010–2020 New Market Tax Credits data; and Opportunity Finance Network 2010–2017 transaction data.

Examples of neighborhoods where investors have deployed concentrations of catalytic capital in pursuit of revitalization outcomes include the following:

- **University Circle.** Through the Greater University Circle Initiative, a concentration of major anchor institutions collaborated in a series of transformative investments in this neighborhood, with the ultimate goal of uplifting a host of surrounding east-side neighborhoods (see box 3).
- **Midtown.** This is an older, east-side industrial neighborhood that helps connect University Circle to Cleveland State University and the downtown. Investments in new housing, human services facilities, transit and neighborhood amenities have sought to bring in new workers and residents while also providing greater opportunities for residents of surrounding low-income neighborhoods.
- **Ohio City.** This neighborhood is separated by the Cuyahoga River from but just west of Cleveland's downtown. Here, a residential renaissance has been underway for well over a decade, supported by a variety of investments in housing and neighborhood amenities.
- **Detroit Shoreway.** In this neighborhood, concessionary financing for a theatre, property tax abatements for developers, and investments in a major lakefront park have helped to spur massive new residential development.

BOX 3

Case Study: The Greater University Circle Initiative

University Circle is a culturally rich neighborhood on the east side of Cleveland. It is host to Case Western Reserve University, the University Hospital System main campus, the Cleveland Orchestra, the Cleveland Museum of Art, the Cleveland Clinic, and over one dozen other significant anchor and cultural institutions. But in the early 2000s, the area was significantly disinvested, and surrounding neighborhoods showed poverty rates of over 50 percent and high levels of property abandonment.

The Greater University Circle Initiative (GUCI) was established in 2005 to physically redevelop the core of University Circle while creating jobs and promoting economic inclusion to benefit surrounding residents. Between 2005 and 2013, there was more than \$140 million of public-private development to rebuild the neighborhood's commercial and residential base, and investment has continued since then. Anchor institutions, foundations, and CDFIs have provided catalytic capital investments through this initiative. While GUCI focused the bulk of its early capital investments on the heart of University Circle, it has expanded investment activity to surrounding neighborhoods over the years, including Glenville, Buckeye, and Fairfax.

A prominent example of the use of catalytic capital in GUCI was the Cleveland Foundation's \$11 million, 20-year program-related investment (PRI) in the \$44 million Uptown mixed-use development in the heart of University Circle. Without that investment, one observer noted, "the risk capital would have been priced much higher and with a much shorter term. You really needed patient capital to move a project like this in a neighborhood that had not seen that level of investment. You have a private developer with a funding gap that only patient, concessionary capital could handle." The total financing package ultimately involved 25 separate financing sources. "Putting together all of the pieces took a lot

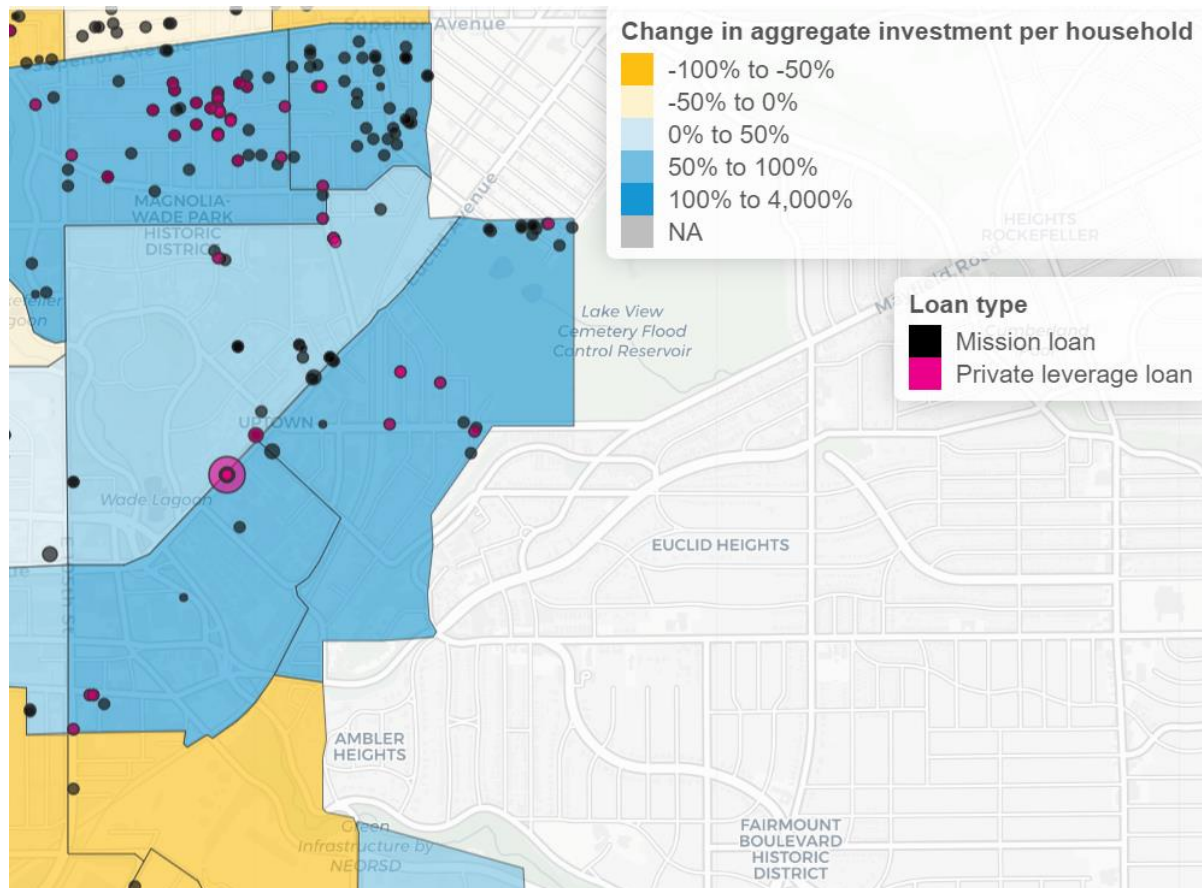
of catalytic capital from the universities, the foundations, and others. If you talk to an older Clevelander, they have seen the change and don't even recognize the neighborhood."

A key observation about GUCI is that while catalytic capital has been invested in the visible and physical transformations of the neighborhood, the key catalytic capital investors in this story have all played other roles beyond those investments. GUCI frames the role of anchor institutions not as capital investors, but rather as major employers and purchasers who can promote equitable development through a "buy local, hire local, live local" strategy. Similarly, while the Cleveland Foundation's case study recognized that "the Foundation can provide seed funding for projects that then leverages larger sources of capital from government and private sources," it cast its primary role as a convener and "honest broker" between stakeholders. Stakeholders in other cities can consider whether this more comprehensive level of engagement and commitment from investors might in fact be a defining characteristic of what it takes for catalytic capital to optimize its impact—or, at times, to have an impact at all.

Our data analysis demonstrates how catalytic capital can lead to increased neighborhood investment more generally. As shown in figure 3, mission-related investments in University Circle associate with private investments that drove an approximately 400 percent increase in annual average total investment per household between 2010 to 2012 and 2018 to 2020.

FIGURE 3

Mission-Related Lending and Change in Annual Average Aggregate per Household Lending in University Circle



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Sources: US Census Bureau 2012–2020 five-year American Community Survey data; City of Cleveland, administrative data; CDFI Fund 2010–2020 Transaction Level Report; CoreLogic 2010–2020 mortgage data; US Department of the Treasury 2010–2020 New Market Tax Credits data; and Opportunity Finance Network 2010–2017 transaction data.

How Catalytic Capital Leverages Neighborhood Investment: Models and Pathways

Because catalytic capital is limited, catalytic investors in neighborhoods seek to maximize their leverage of other sources of funding, especially market financing. We identify three pathways through which this leverage can occur: deal-level leverage, enterprise and fund-level leverage, and neighborhood-level “spinoff” leverage.

Deal-Level Leverage

Catalytic investors can leverage mainstream capital in the capital stacks of projects in multiple ways:

- Provide patient and low-cost capital at a lower return and longer term than mainstream investors would accept, thus allowing a project sponsor to finance more of a project for any given level of cash flow. The foundation PRIs made to finance the Uptown development in University Circle, described previously, are an example.
- Provide patient and low-cost capital as subordinate debt. Subordinate or unsecured financing helps to unlock mainstream capital by assuming a position in the capital stack where it takes greater risk. The Saint Luke's Pointe Campus example in Box 4 below provides an example. Subordinate financing can also be catalytic in the single family mortgage sector: Cleveland Housing Network's CDFI, CHN Housing Capital, provides downpayment assistance in the form of a deferred second mortgage to help homebuyers of modest means, as well as homebuyers moving to targeted neighborhoods. This catalytic capital makes it possible, in turn, for the homebuyer to qualify for a mortgage from a mainstream bank, leveraging as much as 10 times the investment of catalytic capital.
- Provide a loan guarantee or other credit enhancement, removing some or all of the risk to mainstream investors. In Cleveland, the City has made extensive use of the HUD Section 108 loan guarantee program to be able to raise capital for projects such as supermarkets and job training centers. While this example involves a government agency, nongovernmental catalytic capital providers can also provide guarantees and credit enhancements.
- Be the first capital in the life of a project, especially when a project is in the predevelopment phase. As one of our interviewees described, "it is an expensive proposition to get a project to where an investor can look at it. You have this chicken and egg problem where you can't get off the ground." A classic example of catalytic predevelopment capital is the \$200,000 "recoverable grant" that Village Capital CDFI provided to the Capitol Theatre in the Detroit Shoreway neighborhood. This zero percent interest, first-risk investment was structured so that it would be repaid if results from project due diligence were positive and the project could move forward, but forgiven otherwise. (In this case the project moved forward and the funding was repaid.)

For institutional investors who do not have in-house loan underwriting and servicing capacity, provision of catalytic capital at the project level can be challenging. In the case of the Cleveland Foundation's PRI in Uptown, Village Capital manages the investment for the Foundation, facilitating their direct involvement in a project capital stack.

BOX 4

How Catalytic Actors Work Together to Make Deals Happen: Saint Luke's Pointe Campus

The historic, 380,000-square-foot Saint Luke's Medical Center in the Buckeye neighborhood of Cleveland sat vacant for more than a decade following its closure. Cleveland Neighborhood Progress, a citywide community development nonprofit affiliated with Village Capital, led the redevelopment of the campus into an intergenerational learning campus with a charter school, 100 units of market rate, affordable, and senior housing, a Boys and Girls club, a health clinic, a library, an early childhood learning center, and offices for both Cleveland Neighborhood Progress and the Saint Luke's Foundation.⁷ The project was completed in 2012.⁸

The financing process for this redevelopment relied heavily on catalytic capital to make it a reality. It was acquired for \$10 from the city and attracted over \$60 million in investment. One participant said the facility “was caving in on itself. We got the redevelopment done with every alphabet—LIHTC, HTC, NMTC, CDBG. All the foundations were in the deal. So many parts of the deal were completely concessionary—there were grants, there were foundation PRIs ... Village Capital had three loans in the project. We had to build a capital stack where people had to buy into the vision before they could see it. Now we are left with a beautiful campus intended as an intergenerational learning space.” As another participant shared, philanthropies stepped forward to provide catalytical capital, “way before the capital stack for the full refurbishment was there, allowing them to board the place up and maintain it.” Besides investing very early in the project, foundations “had to make concessions so that the ultimate capital stack of the deal could go through.”

Enterprise and Fund-Level Leverage

Catalytic capital providers can also place investments at the enterprise level of a CDFI, in a fund set up by a CDFI, or in another mission-driven financing fund or entity, leveraging other investment in the same entity. To catalyze additional investment in a fund, these investments would be made on flexible terms. For example, investments may provide credit enhancement for other investors (such as through taking a subordinate position in a capital structure or the provision of a guarantee); delivering financing at submarket rates or even zero interest; granting funding that is used as equity or subordinate capital; or using other flexible terms (such as longer terms or no collateral).

JP Morgan Chase, for example, provided a \$5 million grant in Cleveland Development Advisors, a CDFI, through its Partnership for Raising Opportunity in Neighborhoods (PRO Neighborhoods) program. The grant levered an additional \$3.75 million in investment that Cleveland Development Advisors allocated to making below-market loans to developers building projects with high social impact in the Clark-Fulton, Glenville, and Buckeye-Kinsman neighborhoods.

BOX 5

The Role of Catalytic Capital in Jump Starting JumpStart

JumpStart is a 501c3 venture development organization founded in 2004. Its mission is to unlock the full potential of entrepreneurship to economically transform entire communities. It “operates in many ways similar to a combination of a venture capital firm and an economic development entity” per one participant.

JumpStart makes venture capital–like investments in early-stage local technology firms with high growth potential. It also provides significant pro bono technical assistance, grants, and loans to technology startups and more traditional small businesses. Its initial investment capital came from state grants requiring matching funds from other sources. The Cleveland Foundation, the George Gund Foundation, and The Fund For Our Economic Future, among others, provided a mix of grants and PRIs, delivering the necessary match to state grants and loans. This support enabled JumpStart to raise \$70M for its Evergreen Fund.

Today JumpStart partners with for-profit venture and corporate investors to help fund its investment portfolio of 170 startups that have raised nearly \$2B in private capital. The first \$25M of JumpStart's investments have also returned \$82M to advance its mission. In its 2022 impact report, Jump Start reported that it has provided capital or services to a total of 9,433 businesses over its lifetime, 21 percent of which were Black or Latino entrepreneurs. Establishing JumpStart required visionary founding investors willing to take risks mainstream investors avoided. One principal said, “We can now illustrate how investors can generate meaningful financial returns by investing in local early-stage companies—but you could not make that argument 15 years ago.”

Neighborhood-Level “Spinoff” Leverage

Catalytic capital can also seek to leverage private capital investment in nearby properties that are not in the same project or even in the same entity. Here, the theory of change is essentially that catalytic capital can help build the confidence of private market investors in neighborhood markets—whether those investors are big developers, mom-and-pop landlords, or homebuyers. This approach has been fundamental to the revitalization work happening in several Cleveland neighborhoods.

As an example of an investment with what many believe has been a strong “spinoff” effect is the revitalization of the Capitol Theatre in the Gordon Square area of the Detroit Shoreway neighborhood. The \$7.5 million rehabilitation of the property, completed in 2008, used New Markets Tax Credit (NMTC) financing, a \$200,000 recoverable grant from Village Capital for predevelopment work, and a patient loan from the City that has been restructured several times. The theatre brings over 60,000

patrons each year and is “helping to attract new residents, new investment, and ... more foot traffic to support surrounding businesses.”⁹ In purely financial terms, said one of our interviewees, “the loan [to the theatre] generated no ‘return,’ but if you look north from that theatre you will see billions of [dollars of] investment ... If you required that loan to be paid back, maybe the theatre would have gone out of business and none of that investment would have happened.” We note that the Capitol Theatre investment did not happen in isolation. The neighborhood has been the subject of several master plans to coordinate investment,¹⁰ and saw significant public investment both in the revitalization of the Edgewater Park lakefront and in property tax abatements supporting residential development activity.

Indeed, all the neighborhoods where we observe strong neighborhood-level impacts from catalytic capital—not just Detroit Shoreway but also University Circle, Midtown, and Ohio City—have been the subject of sustained, geographically focused investment, supported by multiple actors working together and coordinated by formal neighborhood planning efforts. Between 2005 and 2020, University Circle had the third highest level of mission lending and mission-leveraged private investment of Cleveland’s neighborhoods at \$264 million. These investments helped to drive University Circle’s 380 percent increase in annual aggregate average per capita investment. Detroit Shoreway saw similar mission lending at \$248 million, which helped to drive the neighborhood’s 45 percent increase in annual aggregate average per capita investment. Mission lenders in Ohio City saw a bigger bang for their buck: with \$137 million of MRI, the neighborhood experienced a 162 percent increase in annual aggregate average per capita investment.

It is important to note, though, that not all neighborhoods that received mission investments from 2005 to 2020 saw an increase in total capital flow. A few important factors could be confounding this relationship, including that predatory lending prior to 2008 could be inflating total capital flow values early in our study. Nevertheless, it is clear that there are a handful of Cleveland neighborhoods where catalytic capital did have a neighborhood-level intended effect.

Neighborhood-level community organizations have been playing key roles in leading planning efforts to set the table for catalytic capital investments. An example of this is Midtown, Inc.,¹¹ a community development organization that has crafted a five-year vision for the neighborhood with specific action steps. Midtown, Inc., collaborates with neighborhood associations, anchor institutions, foundations, city officials, and government agencies who coordinate their work through these planning processes.

BOX 6

Neighborhood Revitalization Case Study: Midtown

Until recently, Cleveland's industrial and commercial Midtown neighborhood had been an area with low residential density, few green spaces, and vacant buildings. Despite its proximity to the dozens of medical, educational, and other cultural institutions along Euclid Avenue, it remained underinvested. In 2010, the City of Cleveland and several nonprofit organizations founded the Health-Tech Corridor (HTC), an initiative to develop a health and high-tech business corridor between the anchor institutions located downtown, such as Cleveland State University, and those in University Circle, such as the Cleveland Clinic and Case Western Reserve University. With a focus on equitable and inclusive economic growth, the HTC aims to attract catalytic capital investors to Midtown and surrounding neighborhoods. The City of Cleveland invested \$200 million into the Cleveland Rapid Transit Authority's HealthLine, which was built in 2008 and runs along the entire Euclid Corridor. A person focused on economic development in the Midtown area points to the momentum of the capital brought in by the HealthLine and HTC as an important turning point for the neighborhood: "The HealthLine helped speed the process up" of driving job growth and commercial activity in the area.

The HTC has indeed spurred an outpouring of investment in Midtown. Between 2008 and 2019, over \$335 million of real estate investment in 30 projects has resulted in 750,000 square feet of new or renovated commercial space. Among the projects supported by catalytic capital are the following:

- Manufacturing Advocacy and Growth Network, Inc. (MAGNET) recently opened its new headquarters in Midtown with support from \$5 million in NMTC financing by the Cleveland Development Advisors, a CDFI. MAGNET's headquarters includes space for manufacturing and startup companies, manufacturing education initiatives, and community meetings.
- Dave's Market and Eatery is a 55,000 square foot, full-service supermarket that sits in a former food desert. Dave's offers a pharmacy, food court, space for neighborhood meetings and events, and space for cooking and nutrition classes. Multiple lending partners, including nonprofits, banks, and state and local governments came together to finance the store. Cleveland Development Advisors (CDA), the Northeast Ohio Development Fund, and Capital One provided a total of \$17 million in NMTC financing. The project also received loans from the Ohio Development Services Agency, Cuyahoga County, and the City of Cleveland, as well as a leverage loan from CDA funded in part with a Cleveland Foundation investment.
- University Hospitals' \$26 million Rainbow Center for Women and Children was funded by catalytic capital, also through NMTCs. The Center opened in Midtown in 2018, offering traditional medical care along with community services tailored to the surrounding area, such as nutrition education and legal services.

The Dave's Market was possible because of other developments in the neighborhood that also required catalytic capital. Village Capital Corporation provided concessionary loans to market-rate housing projects as part of a strategy to get a mix of housing that would also attract retail. As one observer reflected, "When you get some density in a place, you can begin to draw some other things, build community assets to benefit all folks." But concessionary capital was needed, even for the market-rate housing projects, to offset the risk to the developer of building for an untested market. Varied housing continues to be created with projects such as the redevelopment of the Warner & Swasey

building into mixed-income housing and office spaces, which will be financed in part by a forgivable loan by the Cuyahoga County Council and an allocation of \$12 million in LIHTCs.

Another driving factor in the revitalization of Midtown has been the decisions by major local institutions to expand into the area. One example is University Hospital's expansion. Another example is the Cleveland Foundation, which announced in 2019 that its headquarters would move from Playhouse Square to Midtown. As an interviewee shared, "The Cleveland Foundation coming in has pushed the boulder over the mountain. The market is starting to take off—people are saying they want to build housing and locate their nonprofit offices here." The Cleveland Foundation is also partnering with JumpStart and MidTown, Inc. to create the Midtown Collaboration Center, which will be adjacent to the Foundation headquarters and will serve as a home for nonprofits and programs by several different institutions such as Case Western Reserve University and the Cleveland Institute of Art. The Collaboration Center was financed in part through \$6.3 million in NMTCs financing by KeyBank.

Community developers are now looking to expand the success of Midtown into the nearby Hough neighborhood, a historically Black and lower income area. A particular focus for these developers is ensuring that long-time residents of Hough and Midtown are being served by the new investment coming in. One interviewee notes that Hough residents have "been here and invested in the neighborhood when it was disinvested, and want to be here to enjoy the neighborhood as it grows." Projects such as MidTown, Inc.'s planned revitalization of the East 66th Street corridor that connects Midtown and Hough will create community-friendly infrastructure that supports increased walkability and provides common spaces for neighborhood engagement. An interviewee also sees an opportunity for catalytic capital to "come in and make sure we are intentional about bringing the rest of the neighborhood along" in creating housing projects to meet various household income levels. One of the projects, Famicos Foundation, is undertaking is the redevelopment of forty homes around the League Park area in Hough that will use LIHTC funding and lead to affordable homeownership through lease-purchase options.

Conditions for Success

While this report has focused on catalytic capital providers, the provision of that capital would not be possible without the engagement and support of two other actors: the investees, who create a pipeline for capital investment, and the public sector, which provides resources and regulates many aspects of development.

Robust Ecosystem of Catalytic Capital Investees

Community development researchers such as Hacke et al. (2013) have highlighted the importance of the “capital absorption capacity” of places—the ability of communities to make effective use of different forms of capital to provide needed goods and services to underserved communities. In turn, these observations have led to increased focus on the organizational “ecosystem” of players that are needed not only to provide catalytic capital, but to plan for, identify, coordinate, develop, and manage a pipeline of deals (Audette, Balbach, and Ashley 2019).

We believe that many of the successes Cleveland has achieved with the deployment of catalytic capital are attributable to the strength of its community development ecosystem and the relationships between key players in it. We do not mean to suggest that Cleveland’s ecosystem is high functioning in every segment or space. But we have been impressed by the range of organizations that engage in neighborhood development throughout the city and the ways that they support one another.

We discussed earlier the strong network of local foundations, anchor institutions, and CDFIs that deploy catalytic capital, as well as the robust city and neighborhood planning efforts that have helped inform this deployment. Equally important is having a strong set of actors generating investable deals. Cleveland enjoys a cadre of about 25 community development corporations throughout its neighborhoods.¹² These organizations “operate where the market doesn’t try to stimulate investment in neighborhoods in a responsible way,” one practitioner said. Another interviewee reflected, “The CDCs take on the ugly, the dirty, the difficult, the challenging—some of the things we take on are things the private sector would demolish from day one.” CDCs thus provide a key partner in which catalytic capital providers invest. The Cleveland Foundation, for example, has provided patient predevelopment dollars for CDCs, which has “allowed us to get our hands on and hold onto property so that we can cue them up for redevelopment,” according to one person we spoke with.

Citywide community development intermediaries play key roles in supporting neighborhood-level organizations. For example, Cleveland Neighborhood Progress not only participates in deals through its CDFI Village Capital, it also supports community planning efforts, provides capacity-building grants and technical assistance to community development organizations, conducts policy and advocacy work, and has its own development arm, New Village Corporation.¹³ Cleveland Housing Network, a citywide housing nonprofit, runs a variety of housing programs and is able to codevelop projects with neighborhood-level developers, as well as provide construction management services to them.¹⁴ Finally, government players have played a key role to set the table for both catalytic and market investment, as we discuss in the next section.

BOX 7

Case Study: Cleveland Housing Network

Cleveland Housing Network, now CHN Housing Partners (CHN), was founded in 1981 as a collaboration of community development corporations (CDCs) to salvage vacant homes and create a pathway to homeownership for low-income neighborhood residents.¹⁵ The Cleveland housing market had been in crisis at the time CHN was formed. As an interviewee shared, “in the 1970s, one of the biggest campaigns the community development corporations ran was an anti-arson campaign [because] ... slumlords were ... not investing.” But at the time, there were only a few CDCs that were doing housing development. Famicos, a faith-based CDC, started doing lease-purchase housing, which provides tenants of rental housing with a path toward owning their housing unit. It then partnered with five other organizations to spread the lease-purchase model. Famicos was the fiscal agent. “It was out of that network where the CDCs said we want to form an organization of equals here—that’s how CHN was formed,” reflected one participant.

Building on Famicos’ success, in 1987 CHN launched a lease-purchase homeownership program using Low-Income Housing Tax Credits. CHN has since developed over 2,189 homes for this program, and CHN reports that about 80 percent of families transition from renting to taking the title of their homes.¹⁶ The organization subsequently expanded into multifamily and permanent supportive housing development and offering as well as variety of counseling, education and other housing services. It has transitioned from being a network organization to its own entity that works both as a CDFI and a developer, as well as expanding its service area. The organization now develops an average of 170 affordable homes each year and serves 50,000 families annually, including in geographies beyond Cleveland.

Catalytic capital has been a driver of CHN’s success. Both the Cleveland and Gund Foundations invested operating support grants in the formation of the organization. Additionally, concessionary debt from both the Cleveland and Gund Foundations helped to finance single family development efforts. “It was maybe 1 or 2 percent interest, 7-year type of money,” recalls an interviewee. “It provided high-risk-tolerant capital for acquisition and development.” Support from both foundations has “never stopped,” adds the interviewee. “They’ve provided support [to CHN] in one form or another for the past 40 or so years. That is what led to the development of scale.”

However, the investment ecosystem is not equally robust throughout all neighborhoods in Cleveland (a dynamic that we think holds in most other cities as well). For example, community development corporations can vary in their capacity due to differences in their staffing size and experience, capitalization and financial strength, and the strength of their relationships with community stakeholders and decisionmakers. CDFIs deploying catalytic capital often have concentrations of deals in particular neighborhoods, for example due to a relationship with a strong housing developer or a

track record in the neighborhood that raises its visibility with capital providers. The unevenness of the capital ecosystem in Cleveland is probably most visible when one considers where anchor institutions are and are not active as investors and catalytic capital providers. Some of Cleveland's most distressed neighborhoods are found in the east side of the city between the downtown and University Circle—the interstitial space that lies just out of the orbit of both major downtown anchor institutions and the University Circle anchor institutions. Changes in capital flows to these neighborhoods have at least in part been driven by changes in the relationship of anchor institutions to these neighborhoods. For example, the recent investments in the Midtown neighborhood suggest that major institutional players recognize that they need to increase their involvement in this part of the city. They also suggest institutional players are expanding beyond University Circle toward the downtown. Neighborhoods that have revitalized without a major anchor institution playing a driving force—such as the Detroit Shoreway and Ohio City neighborhoods—have had to rely upon other market strengths to drive investment.

Government Partnership and Leading Investment

By design, our catalytic capital research has focused on nongovernmental investors, government investment, and leadership that has played a significant role in neighborhood revitalization efforts in the city. In several of the neighborhoods we studied, government-led initiatives have set the table for other catalytic investments that have occurred. Often, these investments have involved local government entities channeling federal funds through mechanisms such as HUD Section 108 or Urban Development Action Grant funds, but they have also included significant tax expenditures (through property tax abatements) and strategic investments of general fund dollars, such as in the city's recent Neighborhood Transformation Initiative. Examples of key public sector investments have included the following:

- Transit investments, such as a \$200 million new bus rapid transit line that is a defining investment of both the revitalization efforts in Midtown and the relocation and renovation of two RTA light rail stops, which were moved and rebuilt to support revitalization efforts in University Circle. The \$200 million investment into the HealthLine RTA route has led to a 10-year payoff of an estimated \$9.5 billion in development along the entire Euclid Corridor, stretching from downtown into the suburb of East Cleveland.¹⁷
- The City of Cleveland has made extensive use of programs including HUD Section 108 and Urban Development Action Grant funds to lend to project capital stacks, including more than \$77 million in loans since 2008 in Greater University Circle Initiative projects.

- Property tax abatements have played a significant role in driving private sector investment, in both large-scale and smaller-scale residential projects. The city’s residential property tax abatement program has been in place for many years, but was recently revised to provide deeper abatements in the most underinvested markets. The program had received some criticism for being too successful and overheating some neighborhood markets (such as Detroit Shoreway), where residents have aired concerns about displacement.
- Metro Parks’ investment in Edgewater Park—which had suffered from significant deferred maintenance until Metro Parks took it over—has been a significant force in the revitalization of the Detroit Shoreway neighborhood.

That said, one stakeholder we spoke with felt it was notable that historically, there have been many instances of the city government and nongovernmental sectors working separately from one another. To the extent coordination increases, there may be opportunities for further leveraging catalytic capital and deepening neighborhood impacts.

Limitations and Constraints

For all of the successes in the deployment of catalytic capital to revitalize neighborhoods in Cleveland, much progress remains to be made. Catalytic capital has driven greater levels of revitalization in some neighborhoods than in others, and has yet to achieve the goal of equitable development across the city. A recent evaluation of the city’s property abatement program concluded, “Cleveland’s housing market [has] remained fragile, with minimal home price appreciation, limited mortgage activity, substantial investor activity, and with many households struggling to make ends meet” (Norton et al. 2020, page a). That said, we also see signs of hope, including a recent estimate that in a reversal of long-term trends, Cleveland is among the fastest-growing metro areas in the US since 2020 (Zhou 2023).

Racial Disparities

We noted at the outset of this report that Cleveland, like other cities we have studied, experiences significant racial disparities in which majority-White neighborhoods receive multiple times the investment per capita compared to communities of color, especially majority-Black neighborhoods. Forces of systemic discrimination that affect mainstream capital markets are undoubtedly a significant factor in the effectiveness of catalytic capital to revitalize a neighborhood. To put it one way, we think that if mainstream capital is twice as likely to go to a majority-White neighborhood than a majority Black neighborhood, then catalytic capital may have to work twice as hard over an extended timeframe to achieve revitalization impacts for Black neighborhoods. But our analysis shows mainstream finance

and catalytic capital are not equally matched, so catalytic capital would need to be 20 times greater to make up for deficits in the provision of mainstream capital. We therefore cannot reasonably expect that catalytic capital or the public sector can reverse racial disparities without the support of mainstream finance.

One historical practice of racial discrimination was redlining—the exclusion of people, households, or companies, by lenders and banks from receiving loans because of their location in low-income neighborhoods or neighborhoods of color, thereby reducing the possibility of investment in those places. Redlined neighborhoods typically have older homes, homes of poor quality, lower homeownership rates, and less provision of mortgage finance. The effects of redlining can be seen in Cleveland today, as a host of health and housing indicators—including access to investment, access to broadband internet, blood lead levels in children, and rental evictions—all follow similar geographical patterns.

Mortgage lending in Cleveland today continues to have high rates of racial disparity. A 2020 study by the Western Reserve Land Conservancy found that the East Side of Cleveland, where 81 percent of the population is African American, had the lowest rate of home improvement loans made compared to other, whiter, Cleveland metropolitan regions such as the West Side, East and West inner suburbs, and the outer suburbs (Ford 2021). On a national level, a study by Freddie Mac found that Black and Latino mortgage applicants received lower appraisals for their homes than the contract price more often than White mortgage applicants (Narragon et al. 2021). This observation stands even after taking other home and neighborhood characteristics into consideration. A low appraisal depresses the mortgage amounts banks are willing to lend, affecting both neighborhood capital flows and homeownership outcomes. One interviewee said, “Banks are conservative about the risk of investing in certain areas. They are more prone to invest in the areas where they feel like they will get their money back. That’s not necessarily redlining, but it can start to look like that after a while.”

Other exclusionary lending practices at work in Cleveland include minimum loan amounts and a general shift to online banking, both of which appear racially neutral but can negatively affect some communities. The Fair Housing Center for Rights and Research points out that since the 2008 foreclosure crisis, median home values in majority-minority neighborhoods in Cuyahoga County are under \$50,000 (Lepley, Mangiarelli, and Simon 2018). Banks often refuse to make mortgages for less than \$50,000, thereby excluding these neighborhoods entirely. Furthermore, the majority of Cuyahoga County census tracts with a broadband access rate of less than 40 percent are located in the urban core and on the East Side of Cleveland, creating a significant barrier for these potential homeowners to switch to online banking or shop for loans online (Arvind and Fee 2016).

Without the public and private sectors addressing both historical and contemporary racial discrimination, catalytic capital alone cannot solve the unique challenges that underserved communities face. To receive the benefits of catalytic capital, communities need more robust and wide-reaching support—for example, in the form of fair housing and lending policy actions, increased broadband infrastructure, or larger amounts of grant and loan money to fund more projects.

Leverage Varies with Neighborhood Market Strength

Neighborhoods in Cleveland have significant variability in market strength: there are large variations in house prices from neighborhood to neighborhood (and even block to block in some places). As of the writing of this report, a single-family home in some parts of the city may cost as little as \$30,000, while a townhome in other parts may sell for over \$500,000.

A handful of neighborhoods—including Tremont, Ohio City, and Detroit Shoreway—are experiencing “high pressure” for potential displacement, as the ratio of neighborhood house price to income in each of these neighborhoods was much higher than citywide (Norton et al. 2020). Yet, in much of Cleveland, where home purchases are made in cash and by investor-owners, these higher-demand, higher-cost neighborhoods see purchases by owner-occupants that are more likely to be funded with mortgage borrowing.

The degree to which catalytic capital will be able to lever mainstream money—whether at the deal level, fund level, or neighborhood “spinoff investment” level—is in part a function of the current market strength of a neighborhood. The stronger the market, the less catalytic capital is needed to make an investment work or to stimulate interest among neighboring property owners. As neighborhoods appreciate, market-rate deals no longer require catalytic capital to be viable. For example, after investing in the first phase of the Uptown project in University Circle, the Gund Foundation found that it did not need to participate in the capital stack for the second phase for the deal to work. But catalytic capital is still needed in strong market neighborhoods to preserve housing affordability or accomplish other socially beneficial projects.

Long Timeframes for the Development of Neighborhood Markets

Neighborhood market strength is malleable, not fixed, but change is typically slow. Interviewees highlighted that many of the neighborhoods that now identified as hot markets with “high pressure” for displacement had markets that were much weaker 20 years ago. One interviewee said, “For every

neighborhood in Cleveland that has gone through significant transformation—like University Circle, Detroit Shoreway, and Ohio City—there was a decade or more, sometimes two decades, of housing investment through community development corporations and the city.” This dynamic is consistent with literature on the long-term cycling of neighborhoods (Rosenthal and Ross 2015) and other place-based efforts across the US that have succeeded in changing disinvested neighborhoods (Theodos 2022a, b, c).

The revitalization of the Detroit Shoreway is a good example of a Cleveland neighborhood that has undergone a decades-long process to build its market strength—a process in which catalytic capital has played a key role. It started around 1980 with the rehabilitation of the Gordon Square Arcade. Prior to this rehabilitation, the neighborhood and the building had fallen into such disarray that the Arcade’s parapet collapsed onto West 65th Street in 1978.¹⁸ Saving the building from demolition required a large amount of concessionary capital including foundation grants and investments, Urban Development Action Grant funding, and CRA-driven bank loans. Further investments included a series of market-rate developments completed by the Detroit Shoreway Development Organization in the 1990s, the revival of a cultural district anchored by the Capitol Theater in 2007,¹⁹ investment in streetscape improvements, and the renovation of Edgewater Park on the shore of Lake Erie. In turn, these investments enticed for-profit developers to enter the market, which helped Detroit Shoreway become one of the stronger neighborhood real estate markets in the city by 2014.²⁰

Catalyzing Small-Scale Investments

Many of the successes that catalytic capital investment has achieved in Cleveland have been with large, highly visible developments, such as the \$44 million Uptown Phase I project in the University Circle neighborhood and several of the projects in Midtown. Catalytic investing in smaller projects like residential infill, small business lending, or home rehabilitation is happening, but is also a work in progress. Many of these projects rely on expensive and scarce subsidy sources such as NMTCs, but they are a finite resource and not efficient for small projects.

Small scale projects are harder for players like foundations and anchor institutions to invest in directly, but fund-level investing is more feasible. Community development corporations, CDFIs, mom-and-pop business owners, and developers are the driving force for such projects. One example is the residential infill development occurring in the Glenville neighborhood led by the Famicos Foundation (a community development corporation and NeighborWorks America network member, not a grantmaking “foundation”). But this work is difficult even for those kinds of organizations. As one

community developer we interviewed put it, “One of the biggest challenges is trying to make neighborhood-scale loans, where the loan size is under \$100,000 or between \$100,000 and \$500,000. But it is risky and hard to do, but that is what will help that apartment building or small, mixed-use property and change neighborhoods.”

Institutional investors seeking to place catalytic capital that can lift up these smaller but critically important projects must scale their engagement. They can do so by providing flexible, enterprise-level investment in and capacity-building support for community development nonprofits. Equitable development outcomes will be hard to achieve without increasing the flows of support to mission finance nonprofits so that they, in turn, can increase small dollar lending.

Small Business Development Challenges

“Catalytic investments have clearly had a significant impact in Cleveland on real estate,” one stakeholder told us, adding that in the case of small business, “it’s hard to point to cumulative impact,” particularly with regard to serving businesses owned by people of color and women-owned small businesses. We did hear of one example of success, a privately funded food accelerator called Central Kitchen that another interviewee told us has “spawned some great companies and been very effective in serving Minority Business Enterprises and Female Business Enterprises as well as generating local employment.”

The overall weakness of the small business development ecosystem in Cleveland is supported by our finding that nationally, Cleveland ranks 92nd out of the 100 largest cities in small business lending per small business employee (Theodos et al. 2023). As a follow-on to this research, we are examining the small business ecosystem in Cleveland, including public, private, and philanthropic support for development services, financing, and procurement. This research will look further into social equity issues in the small business development ecosystem.

There’s Not Enough to Go Around

Several interviewees expressed surprise at our finding that Cleveland had higher levels of mission lending per household than most other major US cities. Their reaction was that there is not nearly enough catalytic capital flowing in the city to achieve the changes they are working toward. We think that both views may be right. Cleveland indeed has a robust system making impressive catalytic capital investments to revitalize neighborhoods. The transformation of areas such as University Circle, Ohio

City, and Detroit Shoreway are testament to the impact of these investments. At the same time, these are just a few neighborhoods, and ones that are poised for investment because of their proximity to major anchor institutions, demographic makeup, or other unique resources (such as the lakefront in Detroit Shoreway's case). Revitalizing more neighborhoods—and especially the most disinvested neighborhoods—will require catalytic capital on a scale that Cleveland has not yet amassed.

Concluding Takeaways for Aspiring Catalytic Investors

For investors in other cities wishing to change neighborhoods through catalytic capital, we offer these recommendations from our examination of Cleveland:

1. Seek deep collaborations with other investors and partners—including foundations, anchor institutions, government agencies, community development corporations, other neighborhood development and planning nonprofits, CDFIs, mainstream banks, and nonbanks. The strongest stories of revitalization that we found in Cleveland involve active engagement from all of these types of organizations. A corollary recommendation would be to invest not only capital in deals but also operating money in ecosystem strength.
2. Support community-based and inclusive planning efforts to guide focused and sustained investment in neighborhoods over time. The more catalytic capital investors can coordinate with each other and align around community goals, the more likely these planning efforts are to be effective and broadly shared.
3. Keep context in mind when setting goals and strategy. Catalytic investment is challenged to reverse broad regional and macroeconomic trends. Moreover, in neighborhoods that face discrimination and in neighborhoods less primed to attract mainstream capital, catalytic capital investors will likely have to work harder to achieve their goals, including investing more and on more concessionary terms. Nevertheless, the Cleveland story demonstrates that catalytic capital can generate meaningful neighborhood gains even in the face of these headwinds.
4. Be patient. The stories of the Cleveland neighborhoods of Detroit Shoreway and University Circle show that catalytic capital can indeed strengthen neighborhoods, even to the point when it is no longer needed, but this process can be a decades-long journey.

Notes

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- ² Brett Theodos, Eric Hangen, Brady Meixell, and Jein Park, “Gauging Investment Patterns across the US,” Urban Institute, May 20, 2021, <https://apps.urban.org/features/capital-investment-flows/>.
- ³ A key limitation of MRIs is that they are subject to the “jeopardizing investment” rules of Section 4944 of the Internal Revenue Code. Risky investments (and foundation managers who approve them) may be subject to an excise tax if the IRS views them as jeopardizing the foundation’s future ability to carry out its exempt purposes.
- ⁴ Paul Brest, “Investing for Impact with Program-Related Investments,” *Stanford Social Innovation Review*, Summer 2016, https://ssir.org/articles/entry/investing_for_impact_with_program_related_investments.
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