Charlotte’s Equity Loan Program: A Model for Financing Inner-City Redevelopment

This article reviews equity loan programs for inner city neighborhoods in Charlotte and Greensboro, North Carolina. The author explains the need for capital in inner cities, then discusses the role of lending in neighborhood development. Three similar programs – Phoenix’s collateral development program, the U.S. Housing and Urban Development Administration’s New Markets Initiative, and the Corporation for Enterprise Development’s Individual Development Accounts – are overviewed and compared with Charlotte’s City Within A City equity program. The author conducts three analyses: 1) an outcome or performance-based analysis, 2) a process analysis of activity interest, and 3) an impact analysis that examines qualitative effects of two business on their respective neighborhoods. Early results suggest that the CWAC program has been successful, although some structural features limit the program’s effectiveness. Self Help has sought to replicate the success of this program in Greensboro. The author provides a set of recommendations for beginning such a program in Greensboro and other North Carolina cities.

Anne Scorza

I. Introduction

Many urban business districts across the United States have suffered over the years from neglect, out-migration of residents and businesses, racial and ethnic discrimination, and public policy favoring suburban development. As a result, these once-thriving commercial and shopping districts, which together with surrounding residential neighborhoods are known as the “inner city,” are now home to vacant or boarded-up buildings, high crime rates, inadequate infrastructure, and struggling businesses. Residents and employees in these neighborhoods do not have access to the goods and services they need, and are thus forced to spend money elsewhere, either in the suburbs or in the city’s more prosperous business districts.

A number of policies and programs have been developed to address these problems. In 1999, the U.S. Department of Housing and Urban Development (HUD) established the New Markets Initiative, designed to stimulate business development in inner cities, which the initiative views as overlooked “new markets” with untapped retail and business potential. Community Development Block Grants, Enterprise Communities and Empowerment Zones, the Community Development Financial Institution (CDFI) Fund, and the Brownfields Economic

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Development Initiative are other federal programs that target investment in these areas. In fiscal year 1996, Federal spending on urban economic development programs for the inner city was approximately $8.9 billion. In 1999, this figure rose to $9 billion. At the state level, state development zones and statewide growth management tools (such as urban growth boundaries) target development by location, environmental features, and socio-economic characteristics.

At the local level, many cities and towns have used tools such as tax-increment financing (TIF) districts, business improvement districts, façade grant funds, and local development zones to meet the needs of their distressed business districts. The City of Chicago, for example, has established over 100 TIF districts, where roads and other infrastructure have been improved, vacant buildings have been rehabbed, and jobs have been created. TIF is a method by which property tax revenue generated from redevelopment is captured and retained for additional redevelopment within the district. TIF can be an effective way to target redevelopment of blighted neighborhoods without diverting the City’s general funds from other projects. (North Carolina’s constitution does not permit the use of TIF programs.)

Likewise, local business owners often use business improvement districts (BIDs) to clean up and provide services to their districts. Under this method, property owners voluntarily agree to pay for common services in the district, usually through taxation. For example, a BID was established in 1992 in Times Square, long known as one of New York City’s red-light districts. The Times Square BID succeeded in using its $7 million annual appropriations, culled from grants, resident dues and commercial building tax assessments, to complete its goal of making the area "clean, safe and friendly," though some have criticized this program for ruining Times Square’s character. Finally, booster groups at all levels of government, through Chambers of Commerce and non-profit organizations, have also formed to promote distressed business district revitalization.

Loan programs are another tool used at the Federal, state and local levels to finance business district development. Governments, non-profit organizations, and private developers often must rely on outside financing to undertake revitalization projects. Likewise, individuals rely on financing tools to start or expand small businesses. For both organizations and individuals, when existing assets are insufficient to fund the project, debt financing is used as a means to leverage existing assets and acquire the necessary remaining funds. Where the gap in existing and needed assets is high, often in inner-city neighborhoods, targeted loan programs can be an effective way to fill the gap and encourage individuals to start or expand businesses. However, a greater challenge exists when equity funds are unavailable. In that case, nothing exists to leverage debt dollars, so it is more difficult to obtain the required debt financing. For many low-wealth individuals seeking to start businesses, it is this lack of equity that hinders their ability to obtain loans.

The City of Charlotte established the City Within A City (CWAC) Equity Loan Program to address this need for equity. By providing deferred equity loans to eligible individuals, the program aims to close the gap between existing and needed assets and thereby stimulate small business start-up and expansion in targeted distressed neighborhoods. The purpose of this paper is to demonstrate the success of this program and to make recommendations for replicating it in other North Carolina cities. Self-Help, a non-profit credit union and CDFI based in Durham, has been an active lender with the Charlotte program since 1995. Recognizing the program’s potential to address the need for entrepreneurial capital in other cities throughout the state, Self-Help has taken the lead in a replication effort currently underway in Greensboro. The replication effort in Greensboro and the program’s experience in Charlotte form the basis of my recommendations.

Before turning to Charlotte’s program and the replication effort, I first explain the need for capital in inner cities, then discuss the role of lending in neighborhood development, and finally briefly discuss three other programs similarly designed to address the need for capital. In Section II, I describe and analyze the Charlotte program as a
case study. The final section of this paper outlines Self-Help’s replication effort and its proposed program for Greensboro, and concludes with recommendations for a successful equity loan program.

The Need for Equity Capital in Inner Cities

Many inner cities across the United States suffer from physical, social and economic distress. Physically, their streets, water/sewer systems, and other infrastructure are often crumbling and outdated. Socially, inner cities have higher crime rates, less educated residents, and a lower skilled workforce than other parts of metro areas. And economically, inner cities have less wealth, less entrepreneurial activity, and less access to capital compared to their suburbs. To contrast these traits with the potential economic advantages of these neighborhoods – such as location and untapped market demand – Harvard Business School Professor Michael Porter identifies these traits as the “real disadvantages of the inner city.”

The focus of this paper is on the last trait: access to capital. According to Porter, "access to debt and equity capital represents a formidable barrier to entrepreneurship and company growth in inner city areas." Hard evidence to support this claim is difficult to find, though some studies do exist. For example, a study of small companies (less than $1 million in annual sales) in the Chicago metropolitan area found that the number of loans to these firms was expected to decrease in census tracts with more blacks or Hispanics and/or with lower income levels. This study, though unable to definitively prove racial or geographic lending discrimination, does show that businesses in lower-income and minority neighborhoods receive fewer loans than those in higher-income and white neighborhoods, controlling for firm size, industry type and firm population. The study also cites research showing that smaller, newer firms are less likely to receive loans than larger, older firms (Cole 1988); black-owned firms are denied loans more often than white-owned firms (Ando 1988); and start-up firms in minority areas receive smaller loans than similar firms in non-minority neighborhoods (Bates 1989, 1993). Finally, a survey by the Initiative for a Competitive Inner City (ICIC) of 40 inner-city businesses in Boston revealed that approximately 60 percent of the business owners reported having difficulty accessing debt and equity capital at the time of the study.

Anecdotal evidence for the lack of access to credit is more prevalent. The Charlotte equity loan program began because of lenders’ observations that access to equity was a significant barrier to loan approvals. City staff agreed that equity was needed, and the City Council approved the program. Throughout Self-Help’s effort to replicate this program, economic developers, City leaders, downtown booster groups, and loan officers in Durham, Charlotte and Wilmington have also pointed to equity capital as the missing piece among many potential borrowers. For example, an informal review of 75 loan applications to Self-Help’s Durham office revealed that six denied loans – nearly 10 percent – would have been approved had equity capital been available. In one case, the loan officer had to deny a loan to an individual seeking to start an ambulance service because “he had weak credit but the real obstacle was that he had no free cash to put into the deal.” While the number of denials may not be large, these six cases show that even for a flexible lender such as Self-Help, lack of equity can be a significant barrier. Furthermore, many potential borrowers are screened out before they reach the application stage, suggesting that an even greater number of individuals do not receive loans because of lack of equity.

There are many explanations for this inability among minority and inner-city firms to access capital. First, discrimination among lenders prevents many minority small business owners from obtaining loans. It is believed that many private lenders practice statistical discrimination, whereby loans to minority applicants are rejected based on historically higher default rates. Second, small loans to entrepreneurs in any environment are less profitable than larger loans, because transaction costs are the same regardless of loan size, while lower interest and fee revenue on smaller loans yields less profit. Lenders therefore prefer to make
larger loans, putting small business owners in the inner city and elsewhere at a disadvantage.

Third, according to Porter, “inner city entrepreneurs often lack personal or family savings and networks of individuals to draw on for capital.” To the extent that Porter’s definition of the inner city includes a large proportion of blacks and other racial minorities, this argument can be supported by evidence that whites have higher net worth and net financial assets than other races. For example, Sherraden (1991) demonstrates that in 1984, the median net worth of whites was as much as 95 times higher than that of blacks and Hispanics. Oliver and Shapiro (1997) likewise show that in 1988, the median net worth—all assets less any debts—of whites was approximately twelve times higher than that of blacks ($43,800 versus $3,700). Finally, a The Wall Street Journal reported in 2000 that white non-Hispanics had approximately six times the family net worth of nonwhites and Hispanics ($94,900 versus $16,400). Whatever the level of disparity, the fact is that nonwhites have significantly less net worth than whites.

Similarly, we can consider net financial assets (NFA)—defined as liquid financial assets that are available for present or future conversion into cash—as another measure of wealth. Oliver and Shapiro find that the disparity in NFA between blacks and whites is even more pronounced than the disparity in net worth: the median NFA of whites is $6,999, while the median NFA for blacks is $0. As expected, this disparity is most pronounced among individuals with less income, education and work experience, and among people younger than age 36 or over age 64.

Less extensive networks of wealthy families or friends also prohibit access to capital among inner-city minorities. Long-time institutional policies have prevented minorities, particularly blacks, from accumulating wealth. Starting with slavery and continuing through reconstruction, Jim Crow segregation, the Federal Housing Act of 1934, urban renewal in the 1960s, and predatory lending today, the financial inequality between whites and minorities has been passed down from generation to generation. Combined with social and other economic inequalities, such as unequal access to education and jobs, the result is that blacks and other minorities have historically had less access to social and financial capital than whites. Therefore, there is less available capital among social networks of minorities than of whites, and minorities, on average, cannot rely on friends or family for capital assistance.

Fourth, Porter argues that “institutional sources of equity capital are scarce for minority-owned companies and have virtually ignored inner city business opportunities.” According to Forbes Magazine, venture capitalists invested $85 billion in developing companies in 1998, but only $2 billion, or 2.3 percent, went to minority-owned companies. Federal government programs leveraged a similar amount of capital for inner-city businesses. ICIC found that in 1996, the Federal government’s $300 million in direct inner-city capital expenditures (primarily in the form of credit enhancement programs) leveraged $2.5 billion in private capital. However, the government spent twice as much ($600 million) on all urban lending programs, which leveraged four times the amount of private capital ($11 billion) as that invested in inner cities. Compared to white-owned businesses and companies located in more prosperous urban areas, then, inner-city businesses receive significantly less equity capital investments.

Charlotte’s CWAC Equity Loan Program was designed to address these shortcomings. Recognizing the specific need for assistance with the equity portion of a project, the loan program’s creators sought to help inner-city entrepreneurs overcome one barrier to small business development. The program was not intended to address the other barriers, such as low credit scores or insufficient business management capability. The City has developed other programs such as the Business and Entrepreneurial Skills Training Program, a partnership with Central Piedmont Community College and First Citizens Bank, to help small businesses address some of these issues. Nonetheless, the CWAC program’s creation and success attest to the need for equity capital among Charlotte’s inner-city businesses.
The Role of Lenders in Neighborhood Development

It is widely recognized lenders play a critical role in neighborhood development and operate in the context of large social, economic, and political forces. The pattern of home mortgage lending over time clearly demonstrates the interaction of these forces. For example, Federal Housing Administration (FHA) and Veterans Administration (VA) loan programs, which created 30-year, fully amortizing, low monthly payment, and 10 percent down payment loans, produced an explosion of home ownership in the United States after World War II. These programs (along with increased home construction and advances in transportation and electric power) also produced a tremendous rise in suburban development. However, another consequence of the FHA and VA loan programs was increased racial segregation between suburbs and cities. The practice of redlining – denying loans to racially-diverse, low-income, high-poverty neighborhoods – which was instituted under the Home Owners’ Loan Corporation (HOLC) during the 1930s, continued under the FHA and VA programs, and was quickly adopted by private banks. The programs also instituted racially restrictive covenants until 1950. As a result of these policies, white suburban home ownership flourished, while blacks and other minorities were increasingly isolated in urban enclaves where property values fell, and lack of investment led to disrepair, vacancy, and abandonment.

Recognizing the ability of loan programs to shape the character of neighborhoods, policy makers can help develop policies and programs to prevent future segregation and dislocation of residents, and produce more economically sustainable neighborhoods. The Community Reinvestment Act (CRA) of 1977 is one such policy. This act requires lenders to serve the neighborhoods from which their deposits come, in order to improve low-wealth communities’ access to credit. To enforce this law, the act requires periodic reviews and requires that Federal regulators consider lending activity to low-income and minority residents when reviewing applications for mergers and acquisitions. Through these reviews, Federal regulators assess lenders’ CRA activity and assign them one of four ranks (Outstanding, Satisfactory, Needs to Improve, and Substantial Noncompliance).

In response to this act and to challenges from community advocacy groups, particularly when banks have sought approval of proposed mergers, banks and other lenders have created CRA agreements and have increased their efforts to target loans to inner-city and other distressed neighborhoods. In the commercial lending realm, CRA agreements can include provisions for lenders to target small businesses, minority- and women-owned businesses, and economic development projects. Despite the serious threat that increased lending to minority and low-income neighborhoods has the potential to inadvertently encourage predatory lending, the Community Reinvestment Act has raised awareness across the country of the important role that lenders play in community development.

One final example further illustrates the role of lenders in neighborhood development. In July 2000, the Forest Conservation Council (FCC) and Friends of the Earth (FoE) issued a joint letter to four regional Small Business Administration (SBA) offices warning that the SBA’s lending activity was contributing to urban sprawl. As a Federal agency, the SBA is responsible under the National Environmental Policy Act (NEPA) to assess the environmental impacts of its actions. According to the letter, FCC and FoE requested that the SBA “prepare a Programmatic Environmental Impact Statement which discloses the cumulative effects of its lending and loan guarantee programs in the Greater Washington D.C. area...since these programs significantly contribute to problems of urban sprawl.” In October, FCC and FoE followed up on their accusation with a lawsuit against the SBA. In response, the national Black Chamber of Commerce filed an amicus brief in support of the SBA. In a similar move, the Small Business Survival Committee (an advocacy group) followed with a counterattack on FCC and FoE, defending the SBA’s loan programs as essential to successful entrepreneurship.

This final example reiterates how dramatically
lending policies can affect neighborhoods and larger-scale urban spatial patterns. Regardless of the outcome of the lawsuit filed against the SBA, this case demonstrates that lending institutions should be aware of the potential impacts of their lending activity on neighborhoods.

The designers of Charlotte’s City Within A City loan program recognize the program’s potential for neighborhood- and city-level impact. By lending in specific geographic areas, in conjunction with the other CWAC initiatives, the equity loan program focuses its efforts on sustainable development of inner-city neighborhoods. To the extent that loans go to businesses in the CWAC targeted area, the program reduces the pressures for urban sprawl. Before turning to this program, I first briefly present three other programs that also address community development and the need for equity capital.

What Others Have Done: Sample Programs

Somewhat surprisingly, there appears to be no other program in the country like the CWAC Equity Loan Program. Many local governments offer low-interest loan programs to stimulate development of targeted communities, but none offers loans deferred up to ten years to small business owners lacking cash for a down payment. The City of Phoenix has a program that is very similar to CWAC, but provides funds for collateral rather than equity. Two other programs addressing the same problem – lack of capital among inner-city business owners – are the New Markets Initiative and Individual Development Accounts. In the following section, I describe these programs, compare them to the CWAC program, and discuss their strengths and weaknesses.

City of Phoenix EXPAND Program

The City of Phoenix established the Expansion Assistance and Development Program (EXPAND) to stimulate access to capital for small and medium-sized businesses. Where the CWAC Equity Loan Program addresses the need for equity capital, the EXPAND program provides financial assistance to business owners lacking adequate collateral to obtain conventional loans.

Under the program, loan applicants who demonstrate all elements necessary to obtain conventional financing except for adequate collateral may apply to the City for a “collateral enhancement.” If approved, the City pledges a Certificate of Deposit (CD) to a participating lender in the amount of 25 percent of the loan (maximum), to a dollar ceiling of $100,000. This CD then serves as collateral for the loan; if the loan goes into default and liquidation, the lender may claim the enhancement funds. However, if the loan is repaid, the enhancement collateral is returned to the program for future commitments. As the loan is paid off, the amount of the collateral enhancement is periodically reduced so that it always equals a constant percentage of the loan amount. These funds – and the interest accrued on them while deposited with the financial institution – are then recycled back into the program.

The EXPAND program is a unique, simple, and effective program to help small businesses obtain loans. From 1993 to 2000, it provided more than $3 million in collateral enhancements to approximately 70 businesses, enabling companies to borrow over $12 million in private funds. On average, the program commits approximately $45,000 in collateral to each business. Since 1993, four projects have defaulted, totaling $97,250, or 3 percent of total funds pledged. Over the program’s seven years, this represents an annual loss rate of less than 0.05 percent, similar to lending industry standards. More than 500 jobs have been created and maintained as a result of the program, the program reports.

The City recognizes the benefits this program creates for the small businesses, citizens and the City as a whole. Business start-up and expansion, increased goods and services, and job creation are among the program’s advantages. Lenders are able to make more loans as a result of the program, thereby increasing profits. The City also benefits from a larger tax base resulting from increased business activity and jobs. The program’s popularity among lenders (16 lenders have used
the program since its inception, 11 from 1989 to 1999) also attests to its success. In addition, the revolving feature of the program makes it self-sustaining. In fiscal year 1998-99, more than two thirds (69 percent) of the program’s funds were recycled from previous collateral contributions and earned interest. (One major shortcoming of the CWAC program is its failure to be self-sustaining, as I discuss later in this paper.)

Challenges and limitations to the program include its reliance on CDBG funds, its broad applicant pool, and its untargeted geography. First, while the majority of the program’s funds come from its own activity, the City may have difficulty procuring CDBG funds annually due to competition for the funds. Second, by not establishing eligibility requirements, the program does not target assistance to those most in need. Third, by allowing loans to businesses anywhere in the city, the program limits its potential to concentrate investment in targeted, distressed areas. However, loans have in fact clustered in City Council District 8 (central Phoenix) due perhaps to a greater need in that area. In addition, the program’s unrestricted geography likely increases political support for the program. EXPAND has been able to successfully balance the need for city-wide political support with the needs of specific neighborhoods, which is crucial for any local government seeking to establish a geographically-targeted program.

New Markets Initiative

Another program similar to Charlotte’s CWAC Equity Loan Program is the New Markets Initiative. NMI is a Federal program launched by the U.S. Department of Housing and Urban Development (HUD) in 1999 to stimulate investment in America’s low-income urban and rural communities. Today, the literature surrounding the initiative focuses on urban communities with a retail gap — where retail buying power exceeds retail sales — that are viewed as overlooked “new markets” with untapped retail and business potential. This concept stems from the research of Porter and ICIC, discussed above, which contends that inner cities have strategic economic advantages over other locations.

The original concept for NMI included seven programs designed to provide technical assistance and capital to the inner city, to create a network of investors, and to increase awareness of the economic potential of inner-city businesses. One program that has received federal funding is the New Markets Tax Credit. This program was enacted in December 2000 and aims to stimulate $15 billion of investment in low-income communities. This program enables qualified community development entities (CDEs) to sell tax credits to investors in exchange for equity capital which the CDEs provide to businesses in qualified low-income areas. Investors receive a tax credit of 5 percent of the investment for the first three years, and 6 percent for the next four years (totaling 39 percent over seven years), plus a portion of the returns generated from the investment. Qualified low-income communities are defined as census tracts with a 20 percent or higher poverty rate, or with a median family income below 80 percent of the area median income. Businesses receiving capital investments from CDEs must be located in, provide substantial services to, or earn at least 50 percent of gross income from these low-income communities.

NMI, and the tax credit program in particular, address the same problem identified by the CWAC program: inadequate capital in distressed urban business districts. Both programs increase the opportunity for businesses in low-income communities to receive loans. Both programs also recognize the potential for inner-city communities to become successful markets for jobs, goods and services, and increased investment. Finally, CWAC and NMI both seek to capitalize on inner-city neighborhoods’ competitive advantages in regards to location, infrastructure, and labor force.

The New Markets Initiative’s strength lies in its recognition of the potential of inner cities, and in its ability to provide information to the public and to investors about this potential. Its involvement of the private sector, through a popular vehicle such
as the tax credit, is another strength.

There are also potential weaknesses and unintended consequences of the initiative and the tax credit program. Most important, the tax credit program runs the risk of causing relocation of neighborhood residents. By enabling non-local businesses to locate in inner cities and qualify for capital investments, and by not requiring employees of these businesses to reside in low-income communities, the program may inadvertently provide more capital to outsiders than to the existing community residents. Also, the program may simply encourage businesses to locate in targeted neighborhoods instead of other areas of the city that may be in need of business development. In this case, business location is diverted from one neighborhood to another, and the city does not necessarily gain a net benefit. Finally, the NMI literature’s focus on retail runs counter to the recognition of the jobs multiplier effect, whereby manufacturing and industrial activity create more jobs than retail businesses. In the case of the tax credit program, where the types of businesses that receive loans and investment will be determined by the CDEs, it will be up to the CDEs to ensure investment in non-retail companies. A provision encouraging CDEs to do this would make sense, such as the provision in the CWAC program that increases the allowable loan amount to manufacturing businesses.

**Individual Development Accounts**

In 1997, the Corporation for Enterprise Development initiated its American Dream Demonstration program to test how well Individual Development Accounts (IDAs) can help low-income and low-asset individuals save and build wealth through the ownership of a home or business, or through investments in post-secondary education or retirement accounts. Michael Sherraden developed the IDA concept, published in his *Assets and the Poor* (1990), as a means of restructuring the American welfare system. Today, 14 demonstration projects run by 13 organizations exist throughout the country to test the concept. The CWAC equity loan program is comparable to the self-employment version of the IDA: both are designed to help individuals overcome the difficulty of saving enough cash for a down payment to start or expand a business.

Typically, an IDA serves as a matching fund whereby every dollar an individual deposits is matched two to one by program dollars. This is the case in North Carolina, for example, where funds are typically capped at $1,000 and matched two to one, according to a study by the University of North Carolina’s Center for Urban and Regional Studies (CURS). When an individual contributes the maximum amount, the program matches it with $2,000, allowing each participant to build up to $3,000 in savings.

The IDA concept is an innovative approach to asset building. By encouraging future-oriented saving behavior, and by limiting the use of funds to specific realms, IDAs address the need for long-term, targeted investment. Sherraden demonstrates that IDAs will benefit not just the recipients at the micro level, but also the nation at the macro level by encouraging economic growth through capital accumulation. What is less apparent, however, is whether IDAs will be a benefit at the neighborhood or community level. In neighborhoods where demonstration projects are underway, will residents have increased access to goods and services as a result of increased capital accumulation? Requirements such as the one in Durham that requires IDA participants to use their savings to purchase a home within certain geographic boundaries are encouraging in this regard.

Among the 14 demonstration programs, more account holders intend to use their funds for home equity than for small business development. On average, 55 percent of the programs’ participants are saving for home purchase, while only 18 percent are saving for microenterprises, according to a study by Washington University in St. Louis. However, as of June 1999, 33 percent of account holders who made withdrawals used their funds for microenterprise, outnumbering the 27 percent of account holders who used their withdrawals for home purchase. The Washington University study
concludes that “early withdrawals for micoreenterprise are common because small sums may be used for small businesses, whereas larger amounts are usually required for home purchases.” Nonetheless, it is encouraging that the IDA program has enabled over 1,000 individuals to accumulate savings averaging $100 per month.30

Summary

Entrepreneurs in many urban business districts in the United States lack access to equity capital. While national programs have been established to address this shortcoming, such as the New Markets Initiative and the IDA demonstration project, very few local programs exist. In targeting inner cities, these national programs shape the way lenders and investors influence specific neighborhoods, and they recognize that lending activity can profoundly affect a neighborhood physically, socially, and economically. Phoenix’s collateral enhancement program and the CWAC Equity Loan Program are two local programs that address these same issues. I now turn to Section II, where I describe the CWAC program and the citywide CWAC initiative, and assess the program’s effectiveness.

II. Case Study: The Charlotte Model

The City Within A City Initiative

In 1991, leaders among the Charlotte City Council recognized that the city’s older urban neighborhoods and business districts were in need of specific, targeted revitalization efforts. Responding to this need, the City formed City Within A City (CWAC), a comprehensive strategy to create a healthy urban core by addressing economic development and quality of life issues in the inner city. Mirroring Charlotte’s local development zones, the CWAC area encompasses 60 square miles surrounding the city’s downtown, and includes 73 neighborhoods. Compared to the rest of the city, which includes approximately 100 neighborhoods covering 240 square miles, the CWAC area’s unemployment rate is currently five times higher, its violent crime rate is twice as high, and its juvenile crime rate is 30 percent higher. The CWAC area also has high poverty, low educational attainment levels, deteriorating and relocating businesses, low quality housing, and low levels of neighborhood involvement and organizational capacity.31

Today, the CWAC initiative is one of five focus areas the City Council has identified to help meet the community’s needs; the others are Community Safety, Transportation, Economic Development and Restructuring Government. The specific goals of the CWAC initiative are to improve the economic opportunity, physical environment, and safety of the CWAC area. To accomplish this, the initiative has attempted to apply the principles of empowerment, sustainability, capacity building, and creating a sense of accountability among community members. Establishing partnerships between the City and community leaders is another important element of the initiative’s mission. As such, the initiative is a comprehensive, participatory approach to neighborhood revitalization.

In order to focus its efforts on the most distressed neighborhoods within the CWAC area, the City set priorities based on income, age, education, and crime data. Later, to more accurately identify the neediest neighborhoods, the City hired the University of North Carolina at Charlotte’s Urban Institute to conduct a comprehensive Quality of Life Study. This study identified 20 variables, shown in Table 1, which were combined by formula into a Quality of Life Index. Weights for the formula are also shown in Table 1. The Quality of Life Index was then used to identify each neighborhood statistical area (NSA) as “stable,” “threatened,” or “fragile.”32

Quality of Life Study Results

The Urban Institute conducted two Quality of Life Studies, one in 1997 and one in 2000. The first study examined only the 73 NSAs within the CWAC boundaries, and used only 18 of the 20 variables. The second study expanded the geographical focus to include 100 NSAs within the Charlotte metro area but outside of CWAC, and used all 20 variables. To account for differences in study areas, and to allow for a more reliable comparison between the 1997 and 2000 studies.
the Urban Institute conducted an additional study in 2000 of only the 73 CWAC neighborhoods. It is important to note, however, that because of the change in variables, a direct comparison of the two studies is impossible. Nonetheless, the Urban Institute is able to conclude that "the strategic shift [from 24 to 30] stable neighborhoods supports the conclusion that CWAC neighborhoods are making substantial strides in community quality of life.\textsuperscript{33}\textedsuper" The results of the studies are shown in Table 2.

In 2000, the fragile neighborhoods formed a semi-circle radiating northeast, northwest, and southwest from the city's core. Threatened neighborhoods extended out from these fragile neighborhoods, and stable areas encompassed most of the study area's outermost rings and the majority of the southeastern corner. The three downtown neighborhoods (First, Third and Fourth Wards) were also ranked as stable. These results typify the pattern of many central cities: a healthy downtown ringed by highly distressed – or fragile – neighborhoods, which in turn are surrounded by healthier, more stable areas.

The CWAC initiative demonstrates Charlotte's commitment to improving the social, physical, and economic well being of its urban core. Its emphasis on community involvement and empowerment is admirable, as is its dedication to tracking neighborhood changes over time through the Quality of Life Studies. The City Council's strategic plan for the initiative is well documented with objectives and measurable benchmarks. For example, under the "business district revitalization" objective, the Council set goals such as "approval of Westover Shopping Center Development" and "Creation of economic development plans for three CWAC retail developments.\textsuperscript{34}\textedsuper" However, the Quality of Life Study is not yet sufficient to evaluate the initiative's success. With future studies, it will be possible to compare results over time, and it will be more apparent whether the program is succeeding in its attempt to increase the number of stable neighborhoods.

The CWAC Equity Loan Program: Description

The CWAC Equity Loan Program is one of several programs specifically designed to meet the needs of the CWAC area. It is managed by the

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Source: Charlotte Neighborhood Quality of Life Study, Table 1. UNC-Charlotte Urban Institute, July 2000.

Table 1: Quality of Life Study Index Variables and Weights
Business Services Officer in the City of Charlotte’s Neighborhood Development Department. The program is one of the City’s ten business financial assistance programs.

The seeds for the equity loan program were sown in August 1990 when Mayor Sue Myrick established the West Side Economic Development Task Force to help promote small businesses on the city’s west side. Meeting with local lenders in November 1990, the Task Force and local banks recognized that lack of capital/equity was preventing inner-city entrepreneurs from obtaining traditional loans. To meet this need, the City of Charlotte’s Community Development Department established the CWAC Equity Loan Program, and expanded its geography from the West Side to include the entire 60-square mile area covered by the CWAC initiative. The City Council approved the program in October 1991, appropriating $1.3 million in City funds from a former Urban Development Action Grant. Eight banks pledged $6.5 million in additional funds. The program began operations on January 1, 1992.

Initially, the City described the program as one designed to create jobs, primarily for low- and moderate-income individuals. Today, the program has four goals:

- To stimulate small business investments in targeted areas.
- To provide low-wealth people access to capital for business start-ups and expansions.
- To create new service and retail businesses to support targeted neighborhoods.
- To create jobs for low-to moderate-income people living in CWAC.

The combination of these four goals is key to the program; the first three focus on neighborhood and entrepreneurial development, while the last emphasizes the expansion of opportunities for others in the area. Together, they seek to address the needs of residents, business owners, and other members of these distressed communities.

**How the Program Works**

Under the program, the City loans the borrower the equity portion of a loan (up to 20 percent of the total loan), and a participating bank provides the remaining 80 percent. The City loan is deferred, with no interest, for a maximum of 10 years, after which interest begins to accrue and repayments begin. Given the time value of money, the zero percent deferment period essentially renders the loan a grant. While the City eventually recoups its money, it forgoes the interest that it would have earned during the deferment period.

When possible, borrowers are expected to commit any available equity funds to the project. For example, if the total project costs for Business A were estimated at $105,000, and the business owner chose to borrow $100,000, then a bank would commit 80 percent of the total loan ($80,000), and the City would commit 20 percent ($20,000). The business owner would pay the remaining $5,000 in personal equity.
Regardless of the dollar amount, the key point is that the maximum allowable City contribution is 20 percent of the total financed portion of the project. However, because the program is based on the recognition that equity is often unavailable, there is no minimum equity requirement, meaning that a business owner could finance 100 percent of the project’s costs. Despite this provision, the City and lender typically request a minimum equity contribution of five percent.

The terms of the loans (as of January 2001) are as follows:

**Total Loan**

- The minimum total loan amount is $15,000.

**City Loan**

- The City loan is subordinated to the bank loan. The City loan repayment is deferred for five years, with the option to renew up to an additional five years if the borrower’s debt coverage ratio exceeds the lender’s guidelines. Repayment to the City begins after the entire bank loan has been paid off, or after the deferment period ends, whichever comes first.
- Interest does not accrue on the City loan until repayments begin; at that point, the market interest rate is charged. However, if borrowers fail to provide information as required in the loan agreement, a market interest rate may be charged during the deferment period.
- City loans are structured so that when repayments begin, the monthly payment equals the monthly payment on the bank loan. As such, the term of the City loan varies.
- Lifetime limits on City loans are $100,000 for non-manufacturing businesses and $150,000 for manufacturing businesses.
- For every $10,000 of City funds borrowed, the business must create one job for low- or moderate-income people living in the CWAC area.
- Loans exceeding $50,000 must be approved by the City Manager or designee; loans over $100,000 must be approved by the City Council.
- Loans involving the acquisition of real estate must demonstrate that the acquisition is required for the viability of the business or for the creation of jobs.

**Bank Loan**

- Banks approve or deny loan applications using standard underwriting criteria. In the event that the equity cash is unavailable, and is the only thing preventing an applicant from obtaining the loan, the bank issues its loan commitment letter with a contingency that the City will provide the additional equity needed in the form of a deferred loan. This is then forwarded to the City, along with the borrower’s personal financial statement, at which time the City processes the request.
- The interest rate cannot exceed prime plus 2 percent.
- Bank loans range from two to ten years. If the lender’s terms exceed ten years, the City’s loan comes due in year ten.
- The bank loan must cover at least 80 percent of the total project cost. The typical bank loan is four times the amount of the City loan.

This structure is an innovative means of fostering business development among entrepreneurs who otherwise would not be able to finance their businesses. By subordinating its lien position to private lenders, the City assumes a high degree of risk. If the program is successful, all City money will be repaid, and banks gain a greater understanding of inner-city areas, a heightened interest in lending to these neighborhoods, and more extensive contact with inner-city entrepreneurs.
Loan Process

Originally, when each participating bank committed money to the loan program, the City would allocate $1 for each $4 committed by the bank. These funds were then available to each bank separately. This system soon became cumbersome, as some banks used their allocated funds quickly while funds reserved for other banks were left untouched and funds could not be easily moved. Today, the program has been streamlined to increase efficiency: the City has established one program fund from which it lends. The City has budgeted approximately $1 million annually for the loan program, which comes from its general fund.

The first steps are key to the loan process. Applicants first approach a participating lender to apply for a loan. Often, the City has referred applicants to a particular lending institution. The lender, using standard underwriting criteria, determines if the applicant is a candidate for the program. According to lenders from two banks active with the program, it is often the geographic location of the business which triggers the lender’s decision to consider the CWAC program.3 If the applicant meets all of the bank’s underwriting criteria except for the required equity, the bank requests funds from the City, which verifies the applicant’s eligibility. If all eligibility guidelines are met and no other source of equity is available, the application will most likely be approved. Once approved, the loan closing process begins, both with the City and the bank. After closing, City and bank funds are disbursed and bank repayments begin.

The process is relatively straightforward and requires little paperwork on the part of the borrower or the lender. When asked about the program, both lenders agreed that the process was easy, and one commented immediately that the process is especially simple compared to the complexity of the SBA’s 7a and 504 loan programs.

Eligibility Requirements and Recent Changes

In order to successfully target the equity loan program, the City of Charlotte has instituted eligibility requirements, dictating where businesses can be located, what types of businesses are allowed, and business owners’ maximum net worth. Over time, these requirements have changed, according to the needs and performance of the program.

The geographic boundaries and net worth cap are crucial components of the program’s ability to reach its target population. For a program with intentions of spurring inner-city development, limiting eligible businesses to designated areas is obviously an important requirement. Also, because net worth is a more effective measure of wealth than income (as discussed in Section 1), a net worth cap will ensure that targeted low-wealth entrepreneurs can make use of this program.

In addition to revisions in the eligibility requirements, the City Council also approved changes to the loan terms in January 2001. These changes are:

- Increasing the maximum bank interest rate from prime plus 1 percent to prime plus 2 percent.
- Reducing the maximum deferral period from ten years to five years, with the option to renew up to five additional years based on the lender’s request (for non-SBA participating loans only)
- Permitting City loans to convert from zero percent interest during the deferral period to a market interest rate when the borrower fails to provide information required under the loan agreement.

These changes reflect three major issues: changes in the lending climate, problems with the program’s original structure, and the politics involved with the program. First, in terms of lending climate, the recent drop in prime interest rates has meant lower profits for lenders; increasing the minimum bank loan interest rate from prime plus one percent to prime plus two percent increases the profit for banks. The City does not anticipate that this will significantly affect loan volume or performance. Second, in terms of program structure, the program manager stated that most
lenders required loan reviews after five years, even for loans with 10- to 15-year terms. During these reviews, it was clear that many of the businesses had been very successful, and could afford after five years to pay off both their bank and City loans. However, with the deferred interest on the City loan, there was little incentive to do this. The reduction in the deferral period addresses this conflict.

Third, the program’s job creation requirements have caused problems from the beginning. In one interview, a borrower complained that the job creation requirement was the most limiting and challenging part of the program. Over the course of one year, this borrower hired thirty different workers, and finally decided to hire her mother to help in her seafood market. Struggling to retain staff, she felt pressured by the program’s job creation requirement. From the City’s perspective, getting the borrowers to annually report job creation data has been equally frustrating. Recognizing that there was no penalty for failing to report job creation data to the City, and therefore little incentive for borrowers to do so, the City added a provision to the program enabling it to charge a market interest rate during the deferment period as a penalty. It should be noted, however, that the City recognizes the frustrations of the business owners. According to the program manager, “It is not a question of actual performance as long as the borrower demonstrates a good faith effort to comply with the job creation requirement. We recognize that business conditions sometimes necessitate changes that will affect earlier projections to create jobs.”

Fourth, the changes to the program’s geographic focus also reflect problems with the original structure, as well as an expansion of the City’s geographic target areas. Originally, the loan program required only that the business hired residents of the CWAC area, but did not require the business to be located within the CWAC boundaries. However, from the beginning it was evident that this requirement was not aligned with the City’s other neighborhood and commercial revitalization programs designed to encourage reinvestment in CWAC. Therefore, in 1998 the guidelines were changed to require that businesses be located in targeted business districts. The expansion of the eligible boundaries to include the Eastside Strategy Plan, the Local Investment Zone, and Morehead Street reflect changing priorities of the City. The CWAC loan program’s ability to adapt to other City goals is an important component of its ability to succeed as part of the larger CWAC initiative.

The CWAC Equity Loan Program: Analysis

A rigorous evaluation of the Charlotte program is beyond the scope of this paper for two reasons. First, the loan program does not work in isolation. The CWAC loan program is part of the City’s larger CWAC initiative, so targeted neighborhoods have received many types of development, infrastructure and safety improvements, education and job training, and other assistance. Also, the CWAC loan program is only one of many small business loan programs available to entrepreneurs in the Charlotte area. Multiple causality therefore limits the possibility of isolating the equity loan program’s effects.

Second, there is no control group to which the affected neighborhoods and businesses can be compared. Without this, it is difficult to attribute any changes in the targeted areas to the loan program. The UNC-Charlotte Urban Institute’s Quality of Life Study may help in this regard. It may be possible to track changes in the status of the neighborhoods where equity loan borrowers are located – for example, to monitor how many neighborhoods change from threatened to stable over time. Subsequent regression analysis might suggest a causal link between equity procurement and neighborhood improvement.

Despite these two factors, an informal analysis of the CWAC loan program can be performed. In this section, I assess the program’s performance to date (outcome analysis) and activity level to achieve its goals (process analysis). I also discuss the qualitative effects of two businesses on their neighborhoods (impact analysis).
Outcome Analysis

The CWAC loan program’s performance can be assessed based on the following indicators: number, size, and status of loans; types of businesses served; number of jobs created; and extent of geographic targeting. Across most of these indicators, the program ranks high and appears to be successful.

Loan Size and Volume

Despite some fluctuation, the CWAC program has demonstrated excellent loan volume over its eight-year history. From 1992 to 2000, the program made 123 loans. Table 3 summarizes the size of these loans. Over the course of the program, the smallest deal was $12,000 (an exception to the $15,000 minimum deal size rule) and the largest was $970,000.

The program averages 14 loans per year. In 1993, 1994 and 1996, the program averaged 16 loans; it made fewer loans in 1995 as the program underwent structural changes, imposed a moratorium, and revised its marketing strategy. In 1997, 11 loans were made, and the following year the program made 25 loans, the largest amount in any one year. In 1999 and 2000, the program made nine loans (see Figure 1). In the first four months of 2001, the program has approved nine loans totaling $400,000, putting the program on track to reach its goal of $1 million for the year.

In the program’s first year, it made only four loans, totaling $223,500. These loans were made over a five-month period, and represent a reasonable loan volume for a new program. However, the program was criticized for approving only four loans because it had over 1,600 inquiries during that first year (the number of loan denials is unknown). Even more significant, however, is the way in which the program was marketed. Low approval levels suggest either overly stringent underwriting guidelines or an unqualified applicant pool; in Charlotte’s case, the first-year applicants were for the most part unqualified and ineligible for the program. Without appropriate targeting and marketing, the lure of the zero percent interest, ten-year deferred loan attracted an overly optimistic and misinformed applicant pool. The Charlotte Observer reported the program’s low approval rate, and the program got off to a rocky start.

After this initial trouble, however, and after working with lenders to more accurately market the program, loan volume picked up. In its nine years, the program has averaged over 14 loans per year, enough to justify replenishing the City’s fund annually with $1 million. The program’s progress since 1996 has been promising, with at least nine loans per year.

Loan Status

Over half of the CWAC loans are still current. As Table 4 shows, 71 percent of City loans have not yet been repaid, mostly because of the deferment period. Because the majority of loans have not yet reached the end of their five- or ten-year deferral periods, the question remains as to how successfully the program will recover its loans in the future.

Eleven loans in this program have been written off. According to the program manager, these businesses failed to pay not because of program characteristics, but because of personal reasons, poor management, or market factors. A local private gym, for example, could not compete with larger gyms in the area; the owner of a lighting company suffered from health problems; and a

<table>
<thead>
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<th>Total</th>
<th>City Loans</th>
<th>Bank Loans</th>
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</thead>
<tbody>
<tr>
<td></td>
<td>$4,044,979</td>
<td>$20,775,160</td>
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<tr>
<td>Mean</td>
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<tr>
<td>Median</td>
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Table 3: Size of CWAC Loans
Figure 1. CWAC Equity Loan Volume 1992-2000

A transportation company failed to renew its contracts with other service providers. These written-off loans, and the loans with assets under review, account for only six percent of the City’s loan funds. While higher than conventional lending programs, this rate is not surprising given the risky nature of the program. Also, this six percent represents a 0.75 percent per year default rate, which is just slightly higher than the industry average (0.5 percent per year).

Businesses Served

Ninety percent of the program’s loans have gone to service and retail businesses, despite its provisions allowing larger loans for manufacturing businesses. Day care centers, restaurants, and hairstyle salons have received the most loans, followed by grocery and general retail stores. Other types of businesses include automotive services, dry cleaning, office supply and professional services, manufacturing, and recycling. This mix of businesses is encouraging, as there is an inadequate variety of goods and services in many of Charlotte’s neighborhoods. From the New Markets and ICIC studies discussed in Section I, it is clear that inner cities nationwide could benefit from a program enabling this extent of retail and service provision. However, manufacturing and industrial jobs are often needed to spur intense economic revitalization of an area (through higher wages and the multiplier effect). To the extent that the CWAC program aims to provide needed goods and services, then, it accomplishes its goal. And by providing local, small-scale retail businesses,

<table>
<thead>
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<th>Status</th>
<th>Number (Percent)</th>
<th>City Funds</th>
<th>Percent of City Funds</th>
</tr>
</thead>
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<tr>
<td>Current</td>
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<td>83%</td>
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<tr>
<td>Paid Off</td>
<td>21 (17%)</td>
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<td>11%</td>
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<tr>
<td>Written Off</td>
<td>11 (9%)</td>
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<tr>
<td>Assets in Review</td>
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<td>1%</td>
</tr>
<tr>
<td>Total</td>
<td>123 (100%)</td>
<td>$4,044,979</td>
<td>100%</td>
</tr>
</tbody>
</table>

Table 4: Status of City Loans
it lessens dislocation pressures. The drawback is that the job potential of the neighborhood may be limited.

The CWAC program makes loans to both new and existing companies. While the breakdown of loans to new versus existing companies for the entire CWAC program is not readily available, an analysis of 22 Self-Help loans reveals that nine loans went to start-ups, ten went to existing companies, and three were used for the acquisition of other businesses. The program’s commitment to new businesses, at least as far as the Self-Help analysis indicates, is promising. Business start-up is especially difficult without personal equity, and it appears that the program has helped entrepreneurs overcome this barrier. Tracking the number of start-ups for the whole portfolio would be beneficial.

An informal review of the CWAC loan portfolio reveals that two-thirds of all loans have gone to African-American borrowers: 17 percent to white borrowers, and seven percent to Asians, Hispanics, and others. 40 Approximately 40 percent of all loans went to women. Among Self-Help loans, the numbers are similar: 82 percent of loans went to minority-owned businesses and 55 percent to women-owned businesses. 41 (According to the 2000 census, 58.3 percent of the City of Charlotte’s population is white.) The program’s high percentage of loans to minorities and women suggests that it has succeeded in enabling both the City of Charlotte and area lenders to meet their mission of increasing loans to those borrowers.

**Job Creation**

Job creation is one of the four major goals of the CWAC loan program. According to the 2000 Job Creation Survey conducted by the City of Charlotte, 66 surveyed businesses created 604 jobs since closing their CWAC equity loans. These businesses received a total of $2,652,097 in City loans, yielding an average of one job for every $4,390. This exceeds the goal of one job per $10,000 of borrowed funds. Twenty-five of the 66 businesses (41 percent) exceeded their job creation requirements. 42

Compared to the SBA’s 503 and 504 loan programs, it appears that the CWAC loan program has performed relatively well in terms of job creation. According to one study of Certified Development Companies receiving SBA 503 and 504 loans, the programs created an average of one job per $8,900 in guaranteed debentures. While this exceeds the SBA’s requirement of one job per $35,000, it is lower than the CWAC program’s performance level. On the other hand, the study acknowledges that all but one of the surveyed companies did not fully comply with reporting requirements, a problem that many CWAC borrowers also experienced (see below). 43 In sum, the CWAC program’s job creation performance on average may exceed the required levels, but it is likely that many of the businesses are unable to sustain the required one job per $10,000 in equity loans.

**Geographic Targeting and Neighborhood Development**

A preliminary analysis of business location and anecdotal evidence from borrowers suggest that the program has been effective at stimulating business activity and community involvement in some neighborhoods, especially where clusters of businesses congregate. Figure 2 shows macro and micro patterns: while businesses receiving CWAC equity loans are dispersed throughout the City Within A City area, some groups of businesses are found in tight clusters.

The size of the CWAC area (60 square miles) does not encourage intense clustering of revitalization activity, although it does not preclude it. How the program is marketed within the vast territory is the key variable. The large area can help build wider political support for the program, although marshalling that support may require considerable effort. This trade-off between geographic/population coverage and focused growth is one that must be carefully weighed. The equity loan program was a natural fit with Charlotte’s larger CWAC initiative, so its large target area is logical. Charlotte’s size and population density also warrant a large target area: 60 square
miles may be necessary to capture the average of 14 loans made every year. However, spreading loans all over town decreases the potential for creating intense revitalization in any one area. Other cities would be well advised to consider this question of scale when replicating the program, and to align their equity loan programs with other development initiatives throughout the city. Smaller cities should consider denser target areas, but should recognize that a minimum geographic area is probably necessary to capture a large enough eligible applicant pool.

Process Analysis

The CWAC program can also be analyzed based on how well its design allows it to achieve its goals or to meet its mission. The program’s greatest strength in this area is its administrative smoothness and simplicity: borrowers and lenders have been pleased with the ease of working with program staff and paperwork, and have praised the program’s management capabilities. Five additional features of the program’s structure have been less effective, and limit the program’s ability to accomplish its goals: the loan approval process, bank participation, job creation reporting, repayment methods, and monitoring and evaluation mechanisms.

Loan Approval Process

The loan approval process for the CWAC Equity Loan Program is relatively straightforward, but at times becomes hindered by politics. As required by law, City loans exceeding $100,000 require City Council approval. To date, this requirement has affected five percent of CWAC program loans, and has at times made the process unnecessarily political and bureaucratic. The story of the Fun City Amusement Park exemplifies the problems of Charlotte’s original loan approval process. John McDonald, the amusement park’s major investor, requested a $142,800 City loan through the CWAC program in 1992. After approval by NationsBank, the City Council rejected the loan with a 5-6 vote along party lines. Republicans opposed the loan, claiming that McDonald, already a successful businessman, did not need the interest-free City loan (the program had no net worth cap at the time). Black leaders responded with charges of racism, and a debate ensued over the purpose of the program, how to determine a reasonable public purpose for use of City funds, and how to determine who needs the City financing. Members of the City Council defended their votes, insisting that McDonald could afford traditional financing and citing Fun City’s cost overruns as reasons to reject the application. This debate received significant media coverage, diverting attention away from the program’s success.

This particular problem would not happen today in Charlotte due to programmatic and political changes. However, any loan requiring approval by an elected body may prove to be politically contentious. While the Charlotte program will not avoid this problem under current North Carolina law, any city replicating this model should ensure that City Councils do not turn into de facto loan credit committees.

Bank Participation

Bank participation, while strong and widespread since the program’s inception, has been inconsistent over time. Twenty banks have participated in the program since 1992. Originally, eight banks pledged a total of $6.5 million in loan funds. Some of these original banks have remained active in the program, and bank participation in general has varied over time. Four lenders – Self-Help Credit Union, NationsBank/Bank of America, Centura and First Citizens – have made over half of the loans. Although less active recently, Self-Help has made the highest number of loans (28), twice as many as any other lender.

Consistent bank participation and positive relationships with lenders are important factors for the program’s success. According to the program manager, high turnover among bank staff in Charlotte and inconsistent bank participation over time have made it difficult to ensure proper marketing and use of the program. Because the
program partly relies on the banks to recognize eligible applicants and forward applications to the City, loan volume is dependent on active bank involvement. Lenders must be committed to understanding how the program works, and remain informed of any programmatic changes. At the same time, program staff must do their part to facilitate working relationships with bankers. A Credit Officer of Scottish Bank, for example, attested to this need. He praised the CWAC program manager for his ability to effectively communicate the program’s goals and needs to bankers, and for maintaining working relationships with the borrowers. This has been key to Scottish Bank’s success with the program, the banker said.

Creating Jobs

The City’s Job Creation Survey indicated that 66 businesses created 604 jobs. While this performance level is good, as discussed above, the program has experienced problems with its job creation and reporting processes. First, program staff have had difficulty compelling borrowers to report job creation information. Borrowers receive letters requesting job information in the first quarter of every year. Follow-up phone calls and additional letters are often required, but eventually the City receives the requested information from 90 to 100 percent of the businesses.55 To encourage borrowers to provide this information, the program decided to charge a market interest rate during the loan deferment period in cases where businesses fail to report job creation (and other) data.

Second, the program requires that employees of businesses receiving loans must be low- or moderate-income residents of the CWAC area. This information is difficult to track and verify. It also limits the number of potential employees, and causes problems when employees move from within the CWAC area to another location.

Another problem is that borrowers have had difficulty retaining qualified staff. One borrower was particularly frustrated with the lack of assistance available to her for finding and retaining staff; she recommended that the City provide a follow-up program, or something in addition to the services of the state Employment office. The City maintains that it refers borrowers to the JobLink Center, neighborhood and business associations, or other small business assistance centers as needed, and in general provides whatever assistance it can to help business owners retain jobs.

Because of the difficulty involved with the accurate reporting of job creation, and because job creation is seen as a low priority goal, Self-Help has omitted a job creation requirement from its proposed equity loan program. This is a prudent idea; job creation is a natural result of business formation, but businesses should not be hindered by bureaucratic reporting requirements. On the other hand, job creation is crucial to neighborhood and economic development, and information on the number of jobs and residence of employees is essential for program monitoring and evaluation. Furthermore, the City of Charlotte contends that its annual job survey allows program staff to stay in touch with borrowers, to assist them with hiring, to “learn about other issues the business owner may be facing,” and to update information in the program’s database.46 This contact is an invaluable part of the program’s ability to monitor its borrowers. However, an annual business review – instead of job reporting – would be an equally effective means of fostering these relationships and obtaining necessary information without causing the problems associated with job creation requirements. As the Charlotte experience has shown, it would also be necessary to institute some level of penalty for businesses failing to participate in the review.

Repayment Methods

As the program is currently structured, loan repayments return to the City’s Development & Revitalization Fund (DARF) and as such, the funds may be used for other neighborhood and commercial revitalization activities. While this funding structure allows the City maximum flexibility, it does not establish a revolving source of funds for the loan program. Accordingly, the program is exclusively reliant on separate annual
appropriations. To address this weakness, the Self-Help replicated model proposes that the fund revolve to the maximum extent possible, recognizing that the deferred repayment structure reduces the revolving nature of the fund. This will decrease the need for additional capital infusions, a feature which could be important in cities with less consistent funding than Charlotte.

Monitoring and Evaluation

The CWAC loan program establishes very little in the way of program monitoring and evaluation. It does require that borrowers send annual reports to the City, including such information as the number of jobs created. However, as discussed above, the City has no way to enforce these regulations, and (until recently) has had no means of penalizing non-compliance. Furthermore, the program has no formal mechanism for evaluating or monitoring its own progress; staff periodically review their progress and determine if changes need to be made. The 1998 and 2001 programmatic changes resulted from staff recognizing deficiencies in the program, and bringing them to the City Council for revision.

The program’s success to date warrants a more formal monitoring and evaluation system. The first step that must be taken is to establish standards by which to measure the program’s progress, and to set more measurable goals and objectives for the future. The only current quantifiable goals, according to the program manager, are 20 loans or $1 million in loans per year, and one job per $10,000 of City loans. It has no goals for gender or race of borrowers, type or location of businesses, or bank participation rates. The program would benefit from setting additional goals, by which it would be able to monitor its impact and progress more effectively. An independent evaluation, perhaps tied to an overall CWAC study, could also be helpful.

Impact Analysis

The third level of analysis involves determining the impact of CWAC businesses on their neighborhoods. Interviews with two borrowers provide preliminary insights into this topic. One borrower, Rita Rondina, used her CWAC equity loan to relocate her silk flower manufacturing business to a larger facility on Charlotte’s west side. The building is located across the street from a public housing development, and further down the street is a new strip shopping center with a day care center. The business, Florita Nova, is also located on public bus routes, and is within walking distance of many residences.

Physically, economically, and socially, this business has made a positive impact on its neighborhood. The building, a former pharmaceutical factory, has been cleaned up, with new windows added on the street level. Landscaping and the addition of a large garden on the side of the building greatly enhance the streetscape. In addition, Rondina makes a conscious effort to attract and retain employees who live in the neighborhood. She has succeeded with this in part because of the building’s accessibility by bus and foot; many of her employees do not have cars. In addition, the business offers English lessons and day care benefits. Rondina has also formed a relationship with a church next to the business. Florita Nova therefore provides quality jobs and important social services to many of the neighborhood’s residents.

As a result of the building’s improvements and the company’s dedication to its physical surroundings, there has been less crime on the formerly vacant street, according to Rondina. Although the 2000 Quality of Life Study ranked the neighborhood as Fragile, improvements to the public housing buildings across the street and the construction of the new shopping area a few blocks away indicate the beginnings of neighborhood change. While this change is not due entirely to CWAC Equity Loan Program, the business it helped to expand certainly has played a key role. Nonetheless, the impact of the loan program and the relocated business is small; the neighborhood can still benefit from economic and physical improvements beyond the scope of the CWAC program.

The West End Seafood Market is also an
integral part of a revitalizing business district less than three miles north of downtown Charlotte. The market’s owner, Bernetta Powell, obtained a CWAC equity loan to start her business in a building formerly occupied by a drug store/restaurant. The building closed in the 1980s and remained vacant, attracting drugs, graffiti and other crime. The City designated the neighborhood as a distressed area, and included it in the CWAC initiative. In 2000, the neighborhood received a Fragile ranking from the Quality of Life Study.[38]

Today, Powell claims her business is having a positive impact on the neighborhood. By providing jobs and a service, the business adds value to the community. Powell also rents out the remaining space in her building to office and retail businesses. Other formerly vacant buildings in the neighborhood have recently reopened. The City has also invested in the area, putting $900,000 into a shopping center located directly across the street from the market, and making over $2 million in infrastructure improvements along Beatties Ford Road. The loan program is therefore an integral part of the City’s comprehensive business corridor revitalization program.

While both Florita Nova and the West End Seafood Market have positively contributed to their neighborhoods, the extent of redevelopment activity that is possible as a result of the CWAC loan program is limited. For example, Charlotte’s physical form will prevent many of its neighborhoods from achieving the new urbanism principles of revitalization. Wide streets with little connectivity and lack of pedestrian-friendly features, for example, characterize Tryon Street and Beatties Ford Road where Florita Nova and the seafood market are located. These neighborhoods are not the vibrant, walkable communities envisioned by new urbanists or the City’s Neighborhood Development Department. Physical and design improvements are needed, which emphasizes how important it is that the CWAC loan program be part of a multi-faceted approach to neighborhood revitalization.

Finally, another significant potential impact of the CWAC loan program is dislocation of residents. As with any program that redevelops an area and raises building and land values, there exists the possibility that current, low-wealth residents will not be able to afford to remain in the area. This threat is palpable in many areas with CWAC businesses. However, the program makes a conscious effort to avoid this by loaning only to low-wealth borrowers, limiting the size of its loans, and requiring that employees who meet the job creation requirements reside within the CWAC area. Therefore, while it is unlikely that the CWAC program alone will cause dislocation of many local residents and businesses, it is important to recognize that the greater redevelopment effort of which it is a part may do so.

Summary

The CWAC Equity Loan Program has been an integral part of Charlotte’s neighborhood development efforts since 1992. It has given over 100 borrowers equity loans to start or expand their businesses throughout the CWAC area, which in turn have provided needed goods and services to Charlotte’s residents, created jobs, and to a small extent helped revitalize communities. From 1992 to 2000, the program performed quite well. A high percentage of loans went to women and minorities for retail and service businesses. The program’s average 14 loans per year were sufficient to give it continued financial and political support. Though most of the loans are still current and the City’s ability to recoup its loan funds is still unknown, repayments so far suggest promising trends for the future.

The structure of the program, while unproblematic for the most part, has imposed some limits on the program’s effectiveness. The loan approval process has the potential to make the program unnecessarily political, job creation requirements are difficult to document and enforce, the loan repayment structure makes the program overly dependent on annual City appropriations, and the program lacks a formal monitoring and evaluation system.

On the other hand, widespread bank participation and positive working relationships with
bankers have helped the program succeed. Importantly, the high quality of the program’s internal management and the straightforward process for borrowers and lenders to use the program have significantly contributed to its effectiveness. While the CWAC loan program could benefit from some structural changes, its performance to date is encouraging. For this reason, Self-Help believes the program can also successfully help entrepreneurs in other North Carolina cities obtain access to equity capital. I now turn to Self-Help’s replication effort and my recommendations for bringing the program to other cities.

III. Replication

Self-Help has been actively pursuing the replication of the CWAC Equity Loan Program since September 1999. Recognizing the potential for the program to stimulate redevelopment in North Carolina’s cities, and the potential to increase its own loan volume, Self-Help staff surveyed its CWAC loan activity in Charlotte, met with Charlotte program staff, and began to consider replicating the program around the state. Using its branch offices in Asheville, Greensboro, Greenville, and Wilmington as guides, Self-Help identified the cities with the most need and the most potential for success. Today, the effort is focused on Greensboro, where plans for a pilot program are underway.

The proposed Greensboro program eliminates the City as manager of the loan fund, but keeps City staff closely involved with program design, geographic targeting, and other programmatic decisions. In place of the City, an independent or quasi-public agency would serve as the loan fund manager, with a steering committee to design and supervise the program.

In this model, Self-Help would be in a unique position to serve as a participating lender, a member of the steering committee, and as the loan servicing and closing agency. This arrangement may involve a conflict of interest for Self-Help, and could potentially put other banks at a disadvantage. To ensure that all lenders have an equal opportunity to make loans, a referral system would be established whereby applicants would be referred equally to Self-Help and other participating lenders.

The Self-Help replication effort serves as a guide for others seeking to adopt the Charlotte program. Replication depends on good timing, community interest, availability of partners and funding, and political support. Even with a good model, Self-Help’s experience shows that replication efforts will confront hurdles. In the sections that follow, I discuss the four primary steps Self-Help took when considering the program – surveying potential cities, identifying key players, developing a budget, and modifying the program’s structure – and offer recommendations for keys to a successful equity loan program.

Surveying Potential Cities

One of the first crucial steps Self-Help took to begin the process of replicating the CWAC program was to identify cities where the program would likely be successful. By nature, the program will be different wherever it is implemented, so it is important to identify the location before finalizing the program’s details. The criteria for an appropriate city, determined largely though Self-Help’s experience in Charlotte and its lending and policy experience in general, include (1) demand for the program, (2) a political culture open to the idea of the program, and (3) a network of organizations – including Self-Help staff, community and economic developers, local government staff, and non-profits – with the capacity and desire to initiate the program. For Self-Help, the logical places to start were North Carolina’s largest cities, where Self-Help has branch locations: Asheville, Greensboro, Raleigh, Durham, Fayetteville, and Wilmington. (Northeastern North Carolina has also been considered for a rural version of the program.)

Visits to these cities and conversations with the key players revealed that Greensboro was the most feasible place to seriously consider the
program. The findings in other cities show how important it is that all three location criteria be met. In Asheville, the community is focused on the need for affordable housing rather than the need for additional small business lending tools. In Wilmington, while the need exists and a variety of organizations were enthusiastic about the program and identified potential funds, the City’s community development department was in the process of hiring a new executive director and therefore lacked the capacity to help plan and implement the program. Finally, Raleigh, Durham, and Fayetteville (together served by one Self-Help branch) each show a need for access to equity capital and the potential for adequate staff and resources, but may be more politically reluctant to accept such a program. Despite these obstacles, these cities should be explored further as possible locations for the program. Currently, Self-Help is focusing its efforts on Greensboro, where conversations with the key players indicated that the timing was right for pursuing the program there.

After identifying the city, Self-Help’s next step was to establish preliminary geographic boundaries, based on poverty, income and other relevant demographic data. In Greensboro, for example, Self-Help mapped the census tracts with poverty rates below 20 percent. These tracts, forming a crescent extending northeast and west from downtown, formed the initial basis for the target area. Other sources that can help identify target areas include state or local development zones, Enterprise Communities or Empowerment Zones, or other geographically defined programs such as Charlotte’s City Within A City initiative. Once these preliminary areas have been defined, the boundaries can be finalized through negotiations with key stakeholders, taking into account the available funds, technical capacity, and political needs.

Identifying Key Players

In conjunction with determining the city and the target area, Self-Help identified the necessary players to be involved with designing, funding, and managing the program. In general, the key players are:

- City staff, likely from the planning, community development or economic development departments;
- Community development corporations (CDCs), non-profit organizations, and foundations;
- Chambers of Commerce;
- Local lenders; and/or
- Small business technical assistance providers

After contacting these entities, Self-Help began to determine the roles and responsibilities for each. In Greensboro, the proposed equity loan fund involves six key players, each with separate tasks. The first, a steering committee, is an informal group similar to an advisory board, and includes members from multiple organizations (banks, City government, non-profit organizations, and Self-Help). The second, a Business Services Representative, is responsible for the program’s administrative tasks and would most likely be a staff member of the third organization, the loan pool fiscal agent. This agent is an independent organization such as the Chamber of Commerce or other local economic development entity. Fourth, technical assistance (TA) providers are needed to help entrepreneurs write business plans and complete loan applications. TA providers can be entities such as North Carolina’s Small Business Technology and Development Center, a small business incubator, local planning departments, or the Chamber of Commerce. The fifth key player is a loan closing and servicing agency. Finally, participating banks are obviously a crucial component of the program. Below are the recommended tasks for each player.

1. Steering Committee
- Assigns and monitors roles
- Drafts written guidelines for loan fund use (e.g., minimum loan amount, net worth requirements, etc.)
- Approves or denies Bank request for program funding
- Has authority to set or change policy
- Acquires funds
- Oversees capital and operating budget
- Evaluates program, reports findings
- Ensures involvement/representation of necessary stakeholders, including low-wealth advocates
- Sets appropriate expectation for loan volume
- Coordinates with entrepreneurial training and real estate development
- Conducts and/or supervises outreach

2. Business Services Representative
- Reviews eligibility checklist
- Coordinates with/participates in bank interactions
- Manages borrower reporting requirements

3. Loan Pool Fiscal Agent
- Maintains loan pool account
- Authorizes loan pool transactions
- Is signatory on loan documents

4. TA Providers/Small Business Assistance Centers
- Provide TA to borrower during loan process and after closing

5. Loan Closing and Servicing Agency (can also serve as a participating bank)
- Closes, services, and records loans
- Prepares program commitment letter

6. Participating Banks
- Promote program availability internally
- Use standard underwriting criteria when considering borrowers
- Coordinate with Business Services Representative
- Provide data for program evaluation
- Assist with outreach, where applicable

Developing a Budget

The next step in establishing the program is to create a preliminary budget and identify funding sources. Using Charlotte’s program as a guide, Self-Help created a ten-year capital and operating budget for the Greensboro program, assuming it would make three to four loans per year. The capital budget projected an average of $53,500 in annual loans, and would require on average $43,500 per year in grants. These figures are based on the assumption that half of the loans made in years one through five will be repaid at a ten percent annual interest rate beginning in year six. On the operating budget side, Self-Help estimates $300 per month in marketing and administrative costs, $15 per month in servicing costs for each loan, and a one-time $250 expense for the approval and disbursement of each loan. Operating revenues would come from a one percent origination fee on each loan, and periodic operating grants.

Once the budget needs are known, the next step is to identify funding sources. Potential sources of funds include the City, the Chamber of Commerce, foundations, government entities, and banks. In Charlotte, the CWAC program was originally funded with a former Urban Development Action Grant. In Greensboro, Self-Help is considering financial support from the City, a local foundation, a CDC, and banks. City funding gives the program political support and helps promote the program’s mission of revitalizing the city’s neighborhoods. However, it is often subject to additional laws such as North Carolina’s requirement that City loan money be approved by the City Council. Foundation and CDC funds are usually more flexible, and for this program are an appropriate means of targeting money to specific neighborhoods in order to help meet the organizations’ missions. Bank funding will in most cases be pledged primarily as a means for the banks to fulfill their CRA requirements, as discussed in Section I of this report. An important question regarding this funding source is whether to require banks to contribute money in order to make loans through the program. Where funding is inadequate, or where competition for program participation is high, this requirement would likely be beneficial.

Modifying the Program’s Structure

The fourth critical step in establishing the program is to modify the CWAC structure to meet the needs and conditions of the new city. Each new location must tailor the basic loan terms, eligibility criteria, and policy guidelines to fit its needs. Before finalizing the details, the program’s
designers can decide the basic terms, such as loan deferral period and maximum loan amount. For example, the Greensboro model proposes a ten-year deferral period, a $250,000 net worth cap, and no job creation requirements. This preliminary structure can be used as a marketing tool to gain financial and political support for the program. Eventually, the steering committee will resolve the details of the program's structure with input from other key players.

Another step in tailoring the program to the needs of each city is to determine the relationship between the key players and the process by which funds will flow through the program. Both of these factors will vary from city to city, depending on local conditions. For example, program funds in Charlotte flow from the City's general fund to the program to the borrowers, and then return to the general fund. The City runs the program, and maintains relationships with banks and technical assistance providers. The Greensboro model proposes that loan repayments return directly to the program loan pool, and establishes a non-City steering committee to oversee the program. Without tailoring the CWAC model to the lending environment of each city, a replicated equity loan program will not successfully meet the needs of its entrepreneurs or the city as a whole.

Next Steps

After identifying the city, key players, funding sources and determining the program’s structure, Self-Help’s next steps to establishing the program will be to convene the steering committee and finalize the details of the program. After that, it plans to obtain commitments from banks, market the program and eventually begin making loans. These general steps can also be taken by other organizations seeking to develop a similar equity loan program.

Recommendations

Self-Help’s replication effort is one of many ways to bring Charlotte’s program to other North Carolina cities. The steps it has taken and the policies that have guided it are unique to Self-Help, but they provide a basis for some general recommendations for a successful equity loan fund. To be successful, a replicated version of the CWAC Equity Loan Program must adapt to the specific circumstances of the city in which it is instituted—its political and institutional climate; any existing programs; the availability of funding, physical space, and infrastructure; its land use patterns; and the economy. Therefore, depending on the timing, location, and organization establishing the program, each program will be different.

The following recommendations can be applied to any city, but are based in large part on Self-Help’s experience in Charlotte and Greensboro. They represent lessons learned over the course of Self-Help’s effort to redefine and recreate a program it believes will effectively facilitate small business development in distressed urban business districts through the provision of equity capital.

Recommendations for Program Structure and Administration

- **Combine the loan program with other city-wide redevelopment initiatives.** An isolated business development/loan program will not improve the physical environment of a neighborhood, the quality of available retail services, or the chance for low-wealth entrepreneurial activity.
- **To avoid politicizing the loan program, ensure that the loan approval process does not require approval of individual loans by elected bodies.** Charlotte’s program received negative media coverage in its early days when the City Council, subject to state law, was charged with approving large loans. It is preferable for an independent professional staff to make loan decisions.
- **Allow loan repayments to recycle back into the equity pool.** This will help the program become more self-sustaining.
- **Set early expectations low.** Do not market the program as a way for any...
low-income individual to obtain a loan. Emphasize that standard underwriting criteria will still be used.

- **Maintain positive working relationships with lenders.** The program requires strong bank participation, and relies on lenders to identify potential borrowers. Lenders must understand how the program works, recognize eligible applicants, and work closely and consistently with program staff.

- **Establish goals or benchmarks for program review and monitoring.** It is important to get feedback from borrowers, to conduct periodic independent reviews, and to perform process, outcome and impact evaluations.

**Recommendations for Eligibility Requirements**

- **Job creation should be seen as a benefit, but not a main goal, of the program.** Job creation is hard to document and verify, and setting goals such as one job per $10,000 is probably unrealistic. It is better to focus on the other important goals of the program, such as improved access to wealth and business development.

- **Require business owners to participate in annual business reviews, and institute a penalty for those who do not.** Information gathered in annual reviews is key to program and business monitoring; it is important to experiment to find the best method for conducting these reviews. Be respectful of business owners' time.

- **Include net worth limit to effectively target a low-wealth population.** The net worth cap is a more effective measure of wealth than income.

**Recommendations for Program Geography**

- **If possible, start with a small target area.** Spreading loans out all over town will not foster synergy from clusters of businesses. Targeting the program to a small, select area will emphasize the program’s geographic focus. Incentives could be included to encourage loans to businesses located near existing program borrowers or desired locations (business districts).

- **Identify a minimum size target area.** While the target area should not be too large, it cannot be so small that the program is unable to make enough loans. It also must be large enough to garner sufficient political support. The program must expand beyond downtown or the area covered by one CDC.

- **Support geographic boundary decisions with census or other data.** Politics and the interests of neighborhood advocacy groups may influence the program’s target locations. To make a more objective decision, identify poverty, income, or other variables that characterize the selected area.

**NOTES**


7 Ibid.


9 Gail McCormick. Email to author. 6 July 2000.


11 Porter, 64-65.


14 Melvin L. Oliver, and Thomas M. Shapiro, Black Wealth/White Wealth: A New Perspective on Racial Inequality (New York: Routledge, 1997): 86. Net worth defined as “the straightforward value of all assets less any debts.”


16 Oliver and Shapiro, 86, 197-199.

17 See Oliver and Shapiro, and Sherraden.

18 Yago.

19 ICIC, 11.


21 Federal Financial Institutions Examination Council rating_faq.htm>.


24 Information on the EXPAND program comes from the City of Phoenix, Community and Economic Development Department, “Innovations 2000” Application; Matt Kane and Peggy Sand, Economic Development: What Works at the Local Level (Washington, D.C.: National League of Cities, 1988); and communications with the program’s administrator.


27 The current literature suggests that dislocation is the more serious consequence of new investment in the inner city, as opposed to gentrification, which can be a positive influx of new capital.


32 University of North Carolina at Charlotte, Urban Institute, Charlotte Neighborhood Quality of Life Study (July 2000) 12. Available <http://www.charmck.nc.us/cindev/qol/Quality_of_Life_Paper.pdf> Neighborhood ranking definitions are as follows: Stable NSAs are those that have few social problems, low rates of crime, few infrastructure and housing needs, and high levels of economic vitality. Threatened NSAs are those that score relatively high on most of the dimensions but may have a significant problem on one or more of the dimensions. Fragile: Fragile NSAs generally have low to moderate scores on all four dimensions. A fragile neighborhood has a lower quality of life and is “at risk” on multiple dimensions.

33 Ibid.

34 City of Charlotte and Mecklenburg County, Strategic Plan,
I interviewed two lenders for this study, in addition to Self-Help staff. The first was Tim Ignasher, Chief Credit Officer of Scottish Bank. The second wished to remain anonymous.

Bernetta Powell. Personal interview. 3 August 2000.

Richard Bargoil. Email to author. 7 Feb 2001.

Jennifer Parker. “City Within A City Loans are Scarce. Critics Ask Why Only a Fraction of Fund Used,” Charlotte Observer 31 Jan 1993: Business, 7C.

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This analysis of Self-Help loans is based only on loans made from 1992-1998.


All information in this section regarding program jobs comes from City of Charlotte, Job Creation Survey: City of Charlotte Business Loan Recipients (FY 2000), unless otherwise stated.

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Ibid. West End Seafood Market is located in NSA 29 (Lincoln Heights).

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