

Unlocking the Development Finance Toolbox

By TOBY RITTNER, CDFA PRESIDENT & CEO
trittner@cdfa.net

As the United States economy begins to pick up steam, state and local recovery efforts will be critical to encouraging the next round of investment, redevelopment, job growth, and sustained economic strength. Paramount to these efforts will be the full utilization of the development finance toolbox to encourage a wide variety of development opportunities. Employing a sound and comprehensive development finance toolbox will ensure that state and local leaders are providing the best resources to address the challenges we are facing today.

What is Development Finance?

Development finance is the effort of communities to support, encourage, and catalyze economic growth. It is a tool to help make a project successful and, in turn, to create an economic benefit for the long-term health of a community's infrastructure, business, and industry. Development finance offers a potential solution to the challenges of the local economic environment. To use development finance tools effectively, practitioners must possess an understanding of the myriad programs, resources, and terminologies that exist in this field. Economic development professionals play an important role as the bridge between government and business. They direct the use of precious public resources, inform policy decisions about how resources are allocated, and act as catalysts for important projects.

What Does Development Finance Include?

Development finance comes in a variety of forms, including loans, equity, tax abatements, and tax credits. It also includes the offer of a guarantee, collateral, or some other form of credit enhancement. Development finance may include gap financing, the remediation of environmental concerns, as well as incentives, grants, or other resources for businesses and entrepreneurs.

Development finance is a proactive approach towards finance intended to assist economic development projects. It leverages valuable public resources to support significant private sector investment. In doing so, development finance helps solve the needs of business, industry, developers, and investors, while also contributing to a community's long-term health and goals.

What Does Development Finance Not Include?

Development finance is not a 'free ride' for businesses in need of assistance. The use of public resources should be tied to accountability measures and project achievements. Unabashed subsidies that provide public contribution while requiring too little private commitment are not considered good practice by professionals.

Development finance tools are not to be applied hastily. Development finance

should be a rational, thoughtful, and strategic response to economic needs and challenges. Community leaders are often placed under considerable pressure to address economic challenges quickly, but a poor development plan may only exacerbate the situation. Insufficient foresight may also lead to unwanted and counter-productive competition with economic development programs in the private sector. Development finance must instead include long-term, strategic thinking.

Why is Development Finance Important?

Development finance is critical to economic development, because financing has the potential to make or break a project. Businesses need access to financial resources to complete a deal. Whether the funds are used for site acquisition or start-up capital, nearly all projects hinge on the borrower's ability to leverage convenient sources of financing. Development finance may offer a type of financing that is less expensive than conventional, private financing.

Development finance is also important because it can benefit all stakeholders. Businesses can use it to generate working capital and invest in their ideas. Developers can use it to achieve an acceptable return on investment (ROI) in a given project. Communities can use it to develop infrastructure, jobs, and amenities.



A well-crafted development finance strategy can balance the needs of industry with the needs of the community.

Why Learn About Development Finance?

Development finance is a complex undertaking. These tools require a considerable amount of knowledge and training, and in many communities, the resources to educate all of the parties involved do not exist. Lack of education and training is a major hindrance to the development finance process, and it can create project obstacles and cause legal problems in the long run. Education is the most critical strategy to make these tools easier to use and understand.

According to CDFA research, 50% of all finance agencies allocate less than 20% of their actual budget to financing development. There are a variety of reasons for this inefficiency, including resources and politics, but education is a significant hurdle for agencies to overcome.

Successful agencies build their programs by educating staff and leadership. Because education requires an investment of resources, development finance agencies must be mindful of allocating funds for this purpose.

The Financing Spectrum

Every economic development transaction presents different challenges. For instance, large-scale industrial development requires a different financing approach when compared to small business development. Typically, development finance is broken down into a spectrum of approaches. Having an understanding of this spectrum will allow development finance agencies to address the needs of established industries, large real estate development projects, small businesses, and individual entrepreneurs.

Some financing options, such as a revolving loan fund, may address a variety of needs and clients. To be effective, however, most development finance efforts must be tailored to a specific need or project. For instance, real estate development does not require the use of start-up capital such as seed or venture capital funding. On the other hand, an early stage entrepreneur is not

likely to benefit from bond financing. Understanding this spectrum is critical to maximizing the development finance resources available in a community.

The Toolbox Approach

Economic development professionals have one of the most difficult jobs in local government: to catalyze investment, to promote opportunity for new and expanding businesses, and to create jobs. This task is further complicated by the fact that although hundreds of programs exist, no one program is a silver bullet solution to economic development challenges. The toolbox approach recognizes the financing challenges facing development projects and seeks to provide realistic and comprehensive solutions.

The toolbox pulls together a variety of programs and offers different tools for the full spectrum of users and projects.

The toolbox approach allows economic development professionals to take a comprehensive approach to development finance by bringing together the best financing concepts and techniques.

The toolbox pulls together a variety of programs and offers different tools for the full spectrum of users and projects. Whether assisting large-scale industrial or micro-enterprise business development, employing the toolbox approach means that an agency will be equipped to act and maximize opportunities for growth in the local economy. The approach also enables a single agency to collect funding at the federal, state, and local government level, as well as from the private sector, all in one place. This comprehensive approach towards the use of public resources is one that is more likely to attract business, investment and growth to a community.

Bringing it Together

Understanding the development finance spectrum is critical to maximizing the resources available in a community. The toolbox approach addresses this spectrum by breaking down dozens of financing options into five practice areas:

- **Practice Area 1: Bedrock Tools**
Bonds and the Basics of Public Finance
- **Practice Area 2: Targeted Tools**
Tax Increment Finance, Special Assessment Districts, Government Districts and Project Specific District Financing
- **Practice Area 3: Investment Tools**
Tax Credits, Seed & Venture Capital and Angel Funds
- **Practice Area 4: Access to Capital Lending Tools**
Revolving Loan Funds, Mezzanine Funds, Loan Guarantees and Microenterprise Finance
- **Practice Area 5: Support Tools**
Federal Economic Development Programs and Tax Abatements

Though not all financing programs fall neatly within these five categories, the toolbox approach is designed to provide a more efficient and effective process for addressing financing needs. The toolbox approach also allows economic development professionals the opportunity to test a variety of strategies on a given project, and to combine programs in order to address financing needs.

Applying the Toolbox

The programs in the toolbox must both adhere to broader public policy goals and allocate precious public resources efficiently. By making programs available to businesses and individuals, a development agency is indicating that these tools have been fully vetted, developed and prepared for use, and that they comply with the guidelines and goals of the agency. Development entities should further consider that when public resources are used to finance projects, the success of these projects is likely to drive future public financing and policy considerations. By bringing together a variety of parties—including banks, thrifts, educational providers, investors, angels and developers—the toolbox approach should help a community reach its ultimate development goal: an expanded capacity to take on new economic development projects.