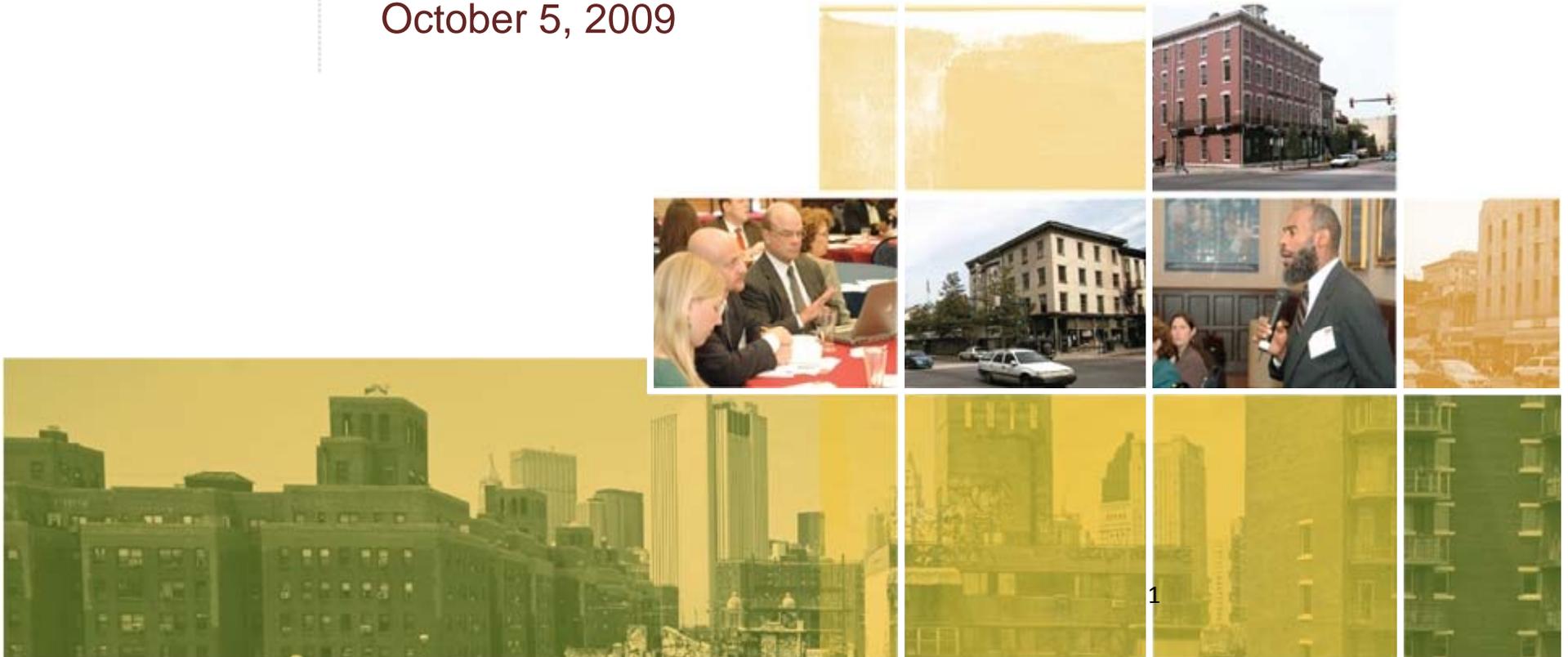




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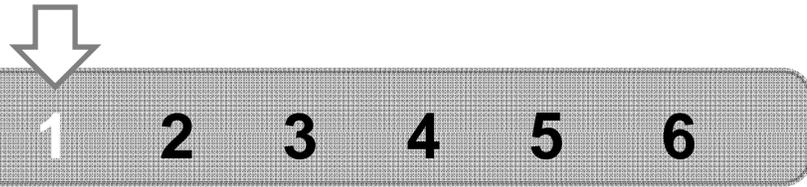
The Federal Role in Supporting Inner City Business Development

October 5, 2009



Summary

- 1 Inner City Challenges
- 2 Inner City Competitive Advantages and Opportunities
- 3 The Performance of Inner Cities
- 4 Factors Impacting Inner City Performance
- 5 Current Federal Programs and Policies for Inner City Business Development
- 6 Federal Policy Reform for Inner Cities



Inner cities face serious poverty and related challenges that can be alleviated through business development strategies.

Inner cities, by definition, are urban cores with high poverty and unemployment rates and low median income levels.



We define **inner cities** as contiguous census tracts in central cities that are economically distressed with:

Two of the three criteria:

Poverty rate
20% or higher

or

• Poverty rate 1.5x times or more than their MSA

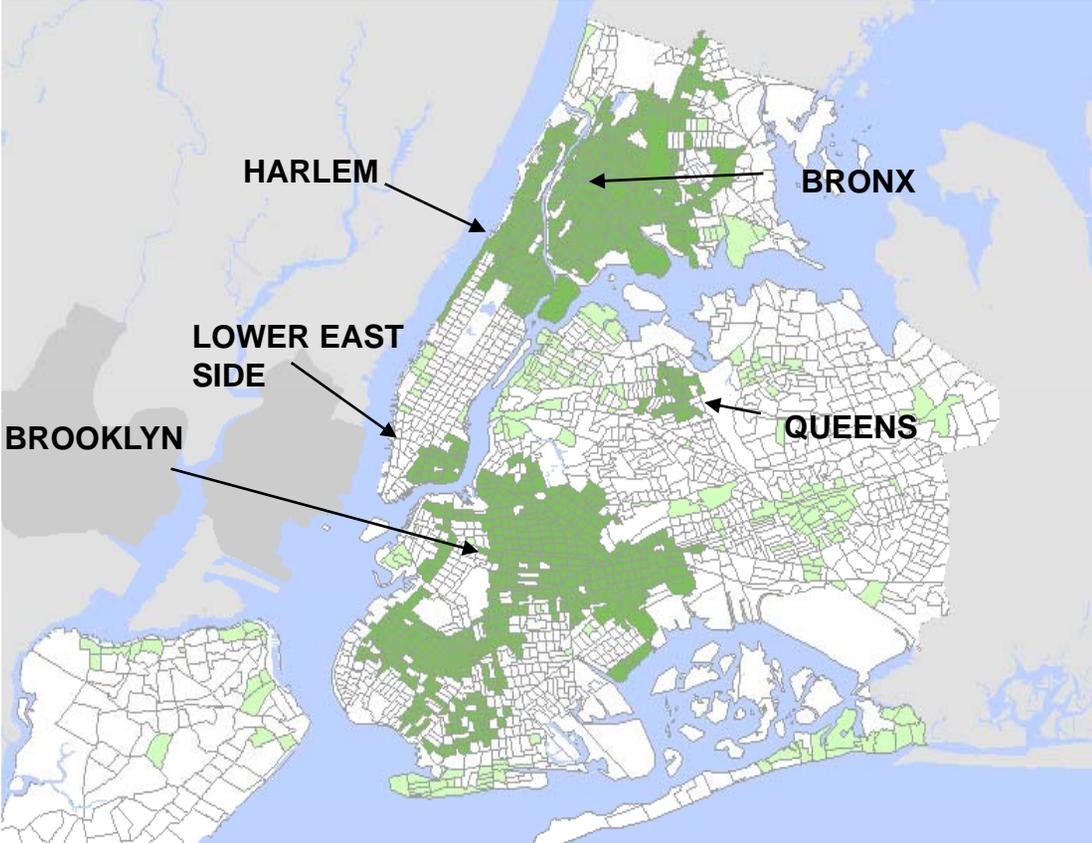
• Median household income ½ or less than their MSA

• Unemployment rate 1.5x or more than their MSA

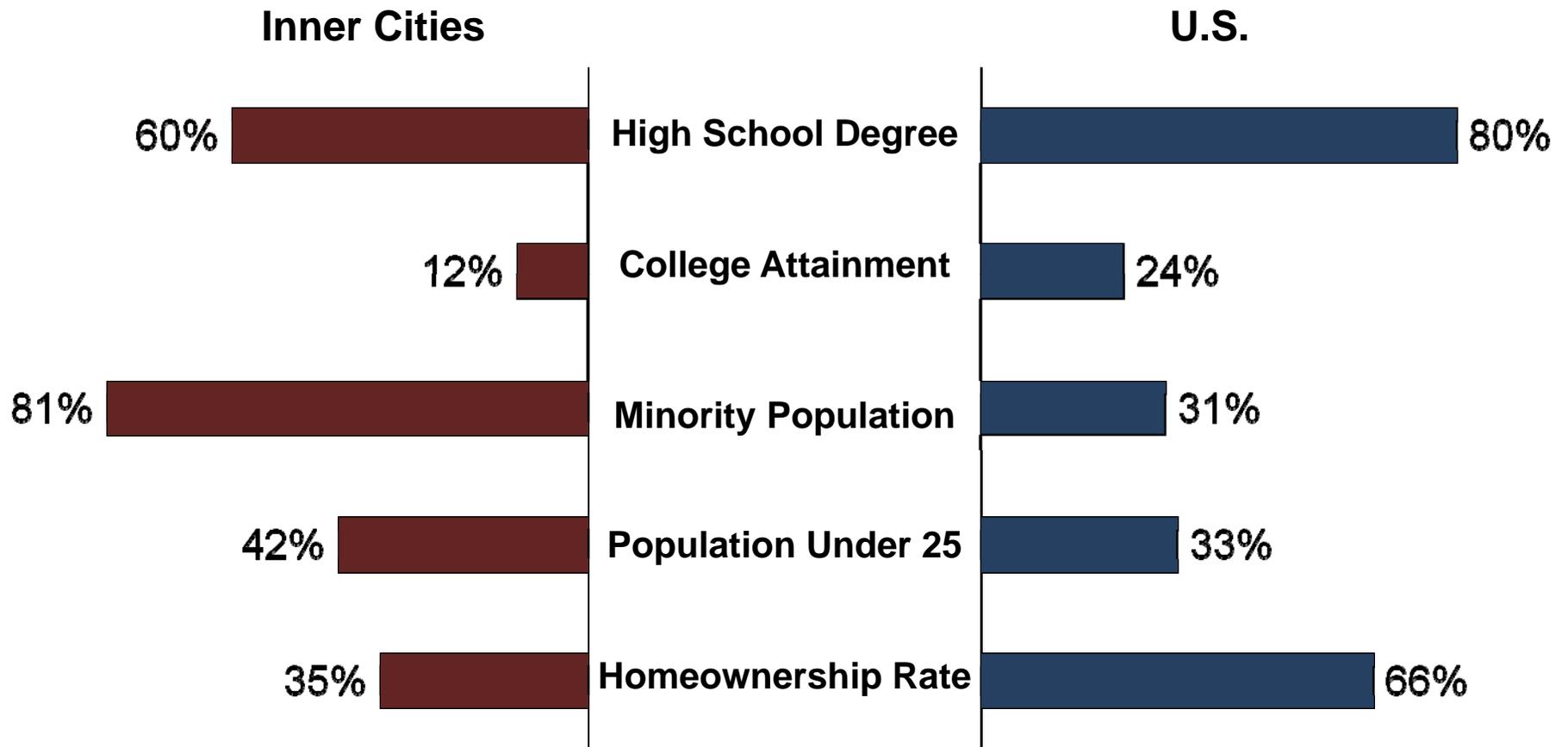
We track the performance of the inner city portion of the 100 largest central cities in the U.S.

➔ These 100 central cities account for two-thirds of total U.S. central city population.

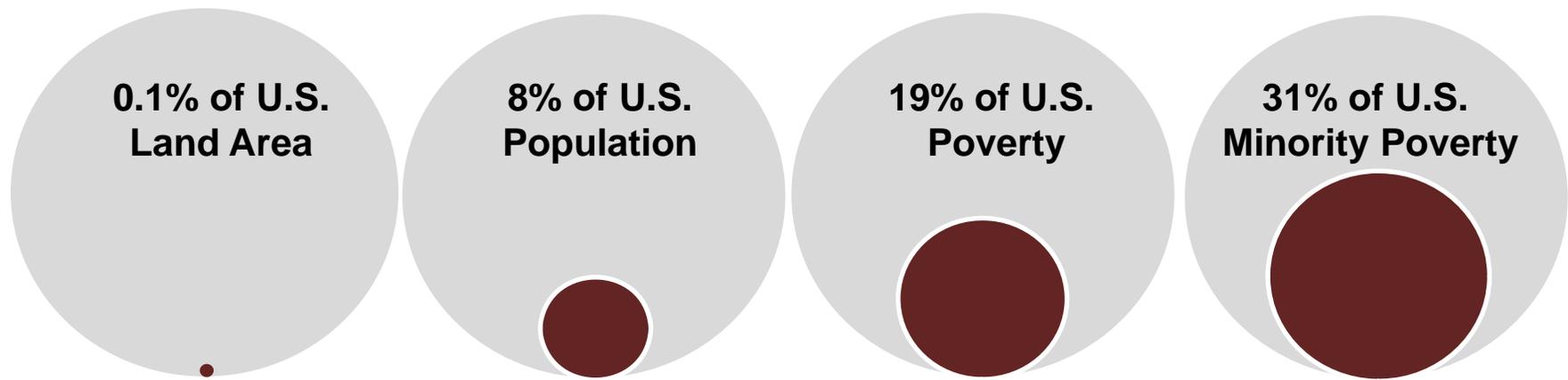
Example:
New York's
Inner Cities



Inner cities have lower educational attainment levels and a younger and more diverse population than the rest of the U.S.



Inner cities are also home to one-fifth of U.S. poverty and one-third of minority poverty.



Through business development and job creation, the federal government can target poverty more effectively.

Solution to
Poverty



Shift emphasis from the consequences of poverty: transfer payments, Medicaid, etc.

to

Job Creation and Firm Formation

- Starting and owning businesses, as well as moving up the management hierarchy, are the only ways to build income and wealth in inner cities.
- Inner city economies will not prosper by a focus solely on regional economies - they have special economic issues and opportunities.

....we need a strategy focused on these areas.

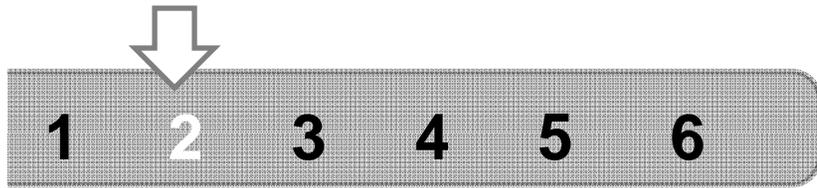
“Jobs anywhere” are not enough. Often inner city residents cannot access jobs in the rest of the region.

In a typical U.S. region inner city residents hold:

- 22% of the jobs in the inner city
- 11% of the jobs in rest of the central city
- 7% of the jobs in the rest of the region

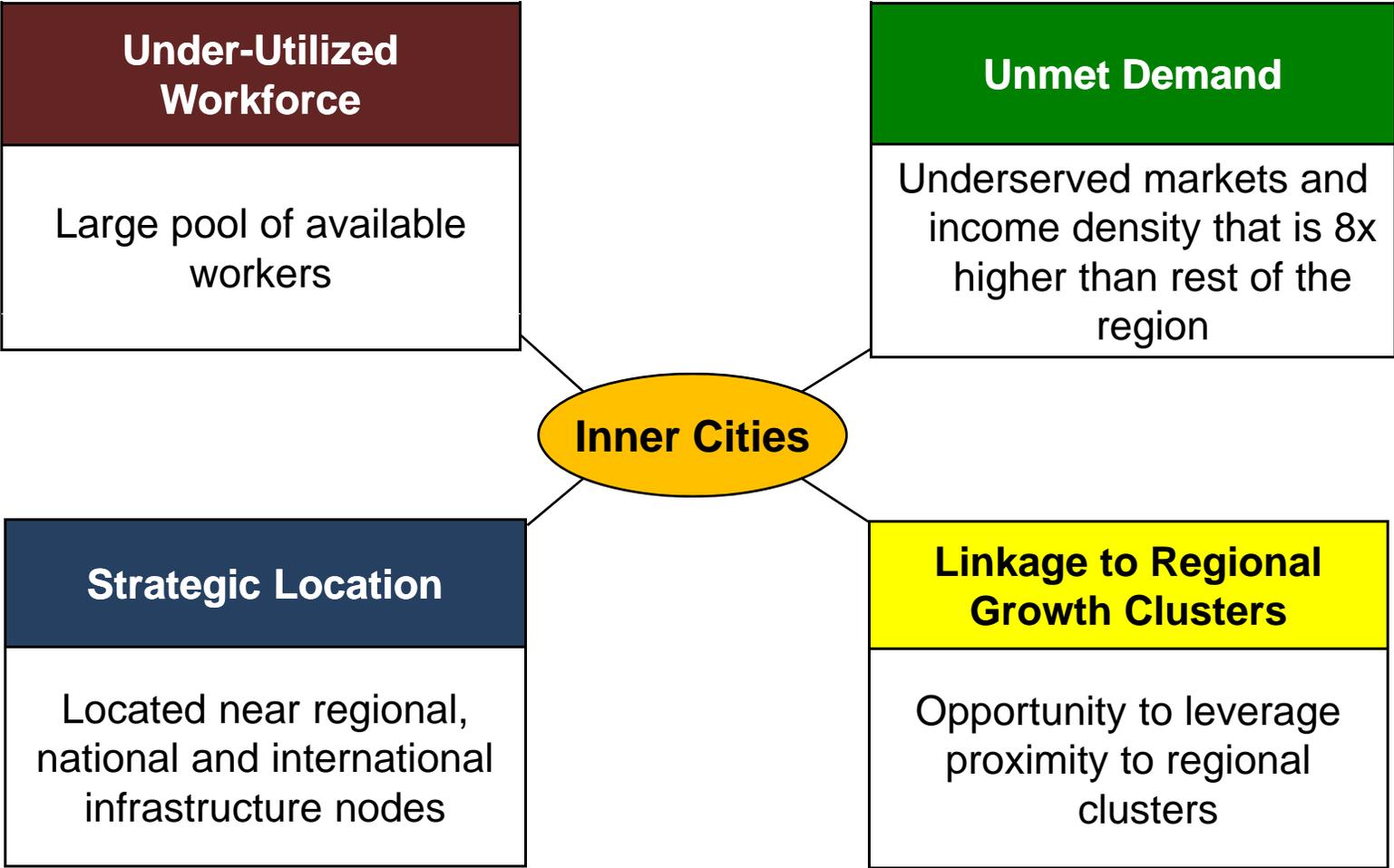
Creating 1,000 new jobs for inner city residents would require:

- 450 jobs in the inner city
- 850 jobs in the rest of the central city
- 1,450 jobs in the rest of the region

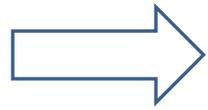


Inner cities have many competitive advantages and offer important investment opportunities.

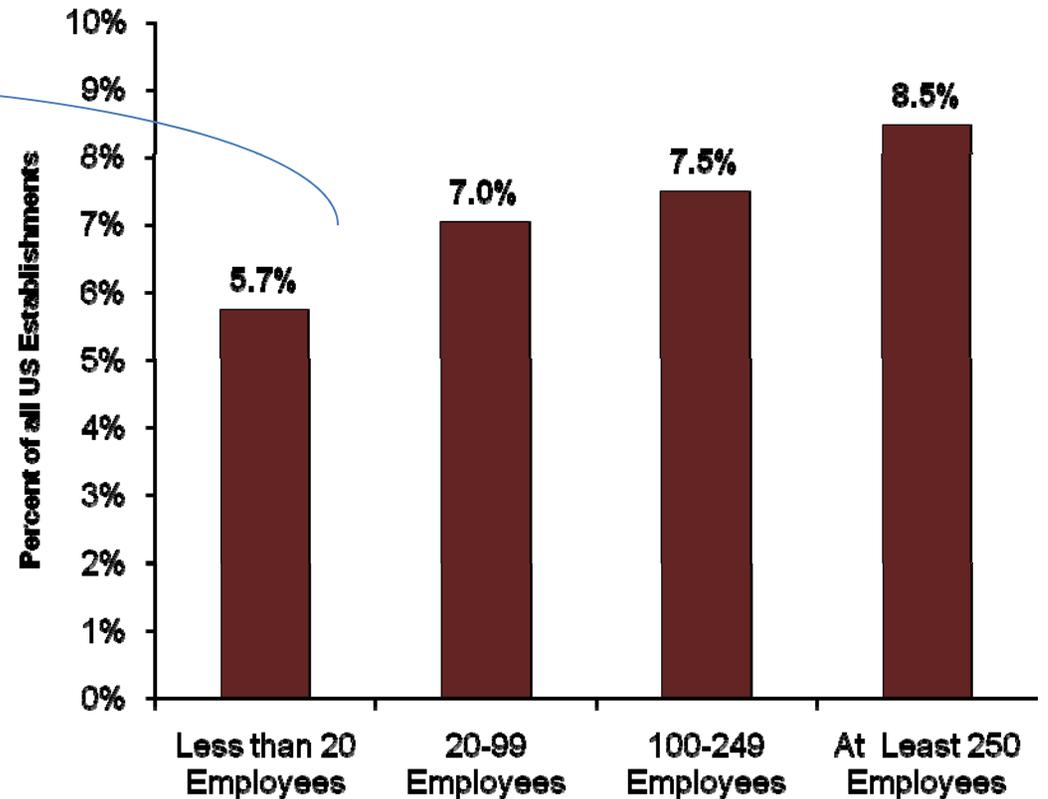
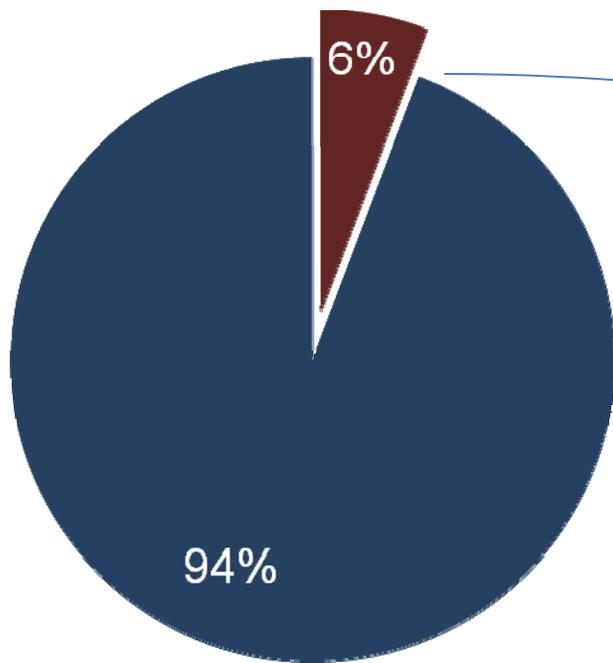
Inner cities have numerous competitive advantages, but the scale and intensity varies from place to place.



Inner city firms are home to 6% of U.S. firms and over 7% of U.S. employment.



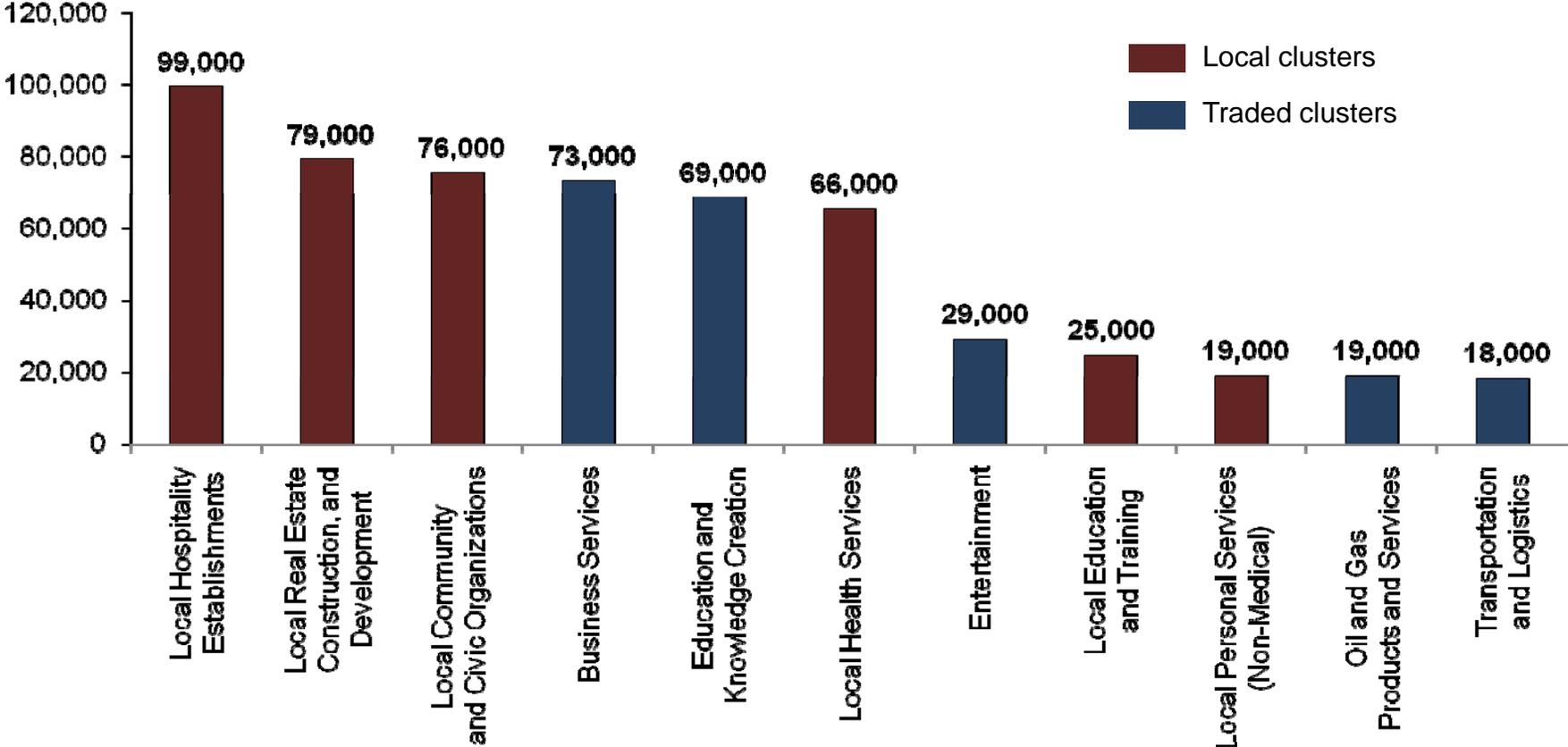
Inner cities businesses in the largest 100 inner cities employ more than 8.8 million workers



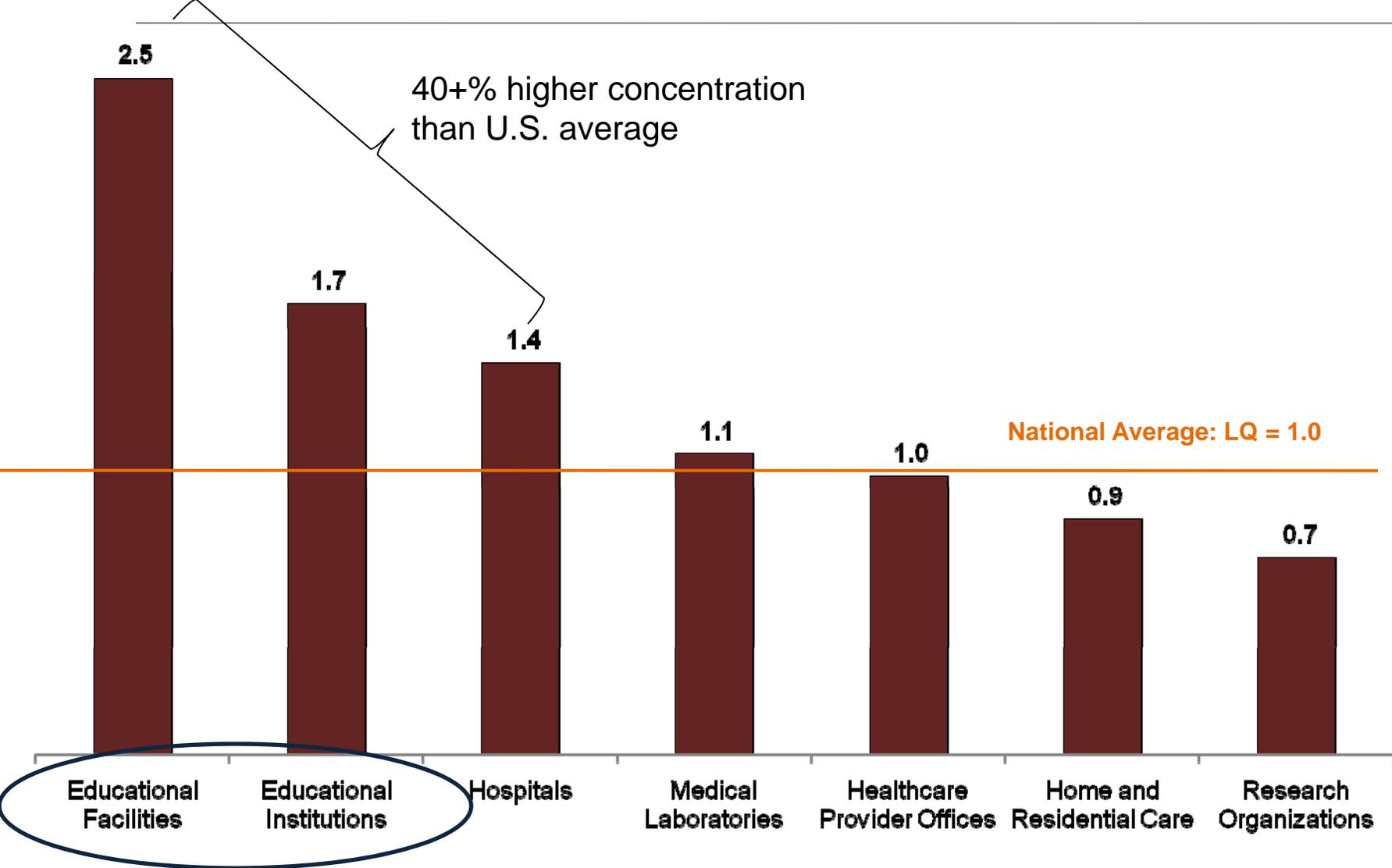
Inner cities have experienced strong growth in some clusters, including business services and education.



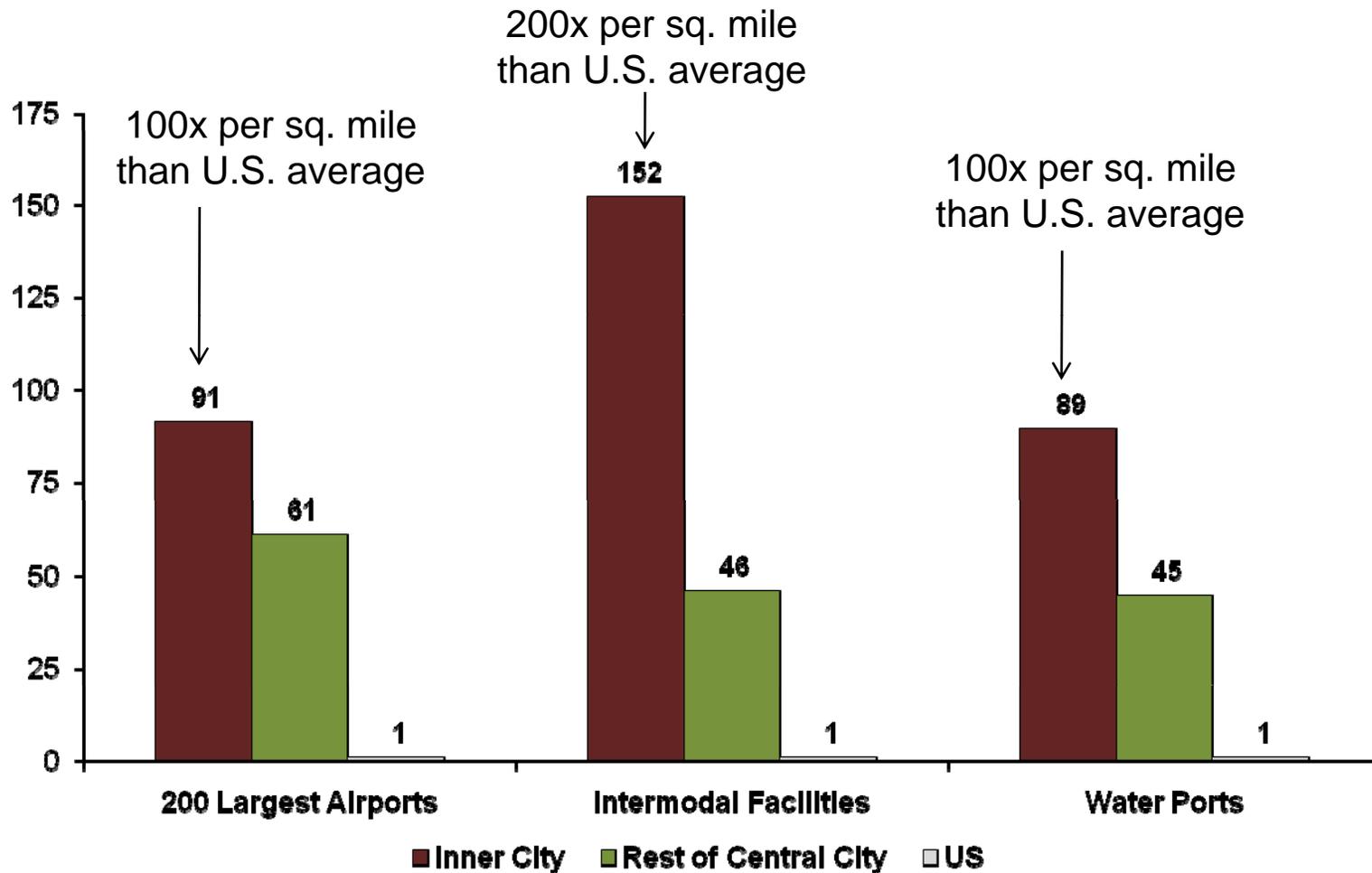
Inner cities have strengths in both local and traded clusters.



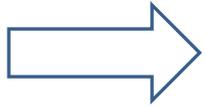
Inner cities have high concentrations of educational and medical institutions.



Inner cities have significant concentrations of infrastructure assets.

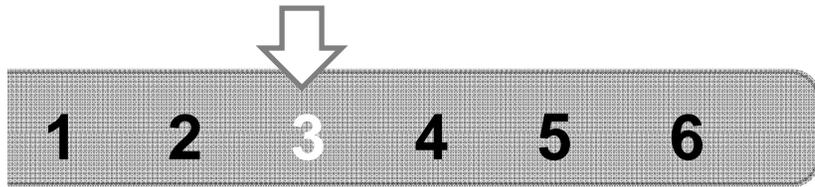


Large tracts of land are an emerging competitive advantage in urban areas.



The projected 10-year vacated building space in urban areas across the U.S. is over 1 billion square feet.

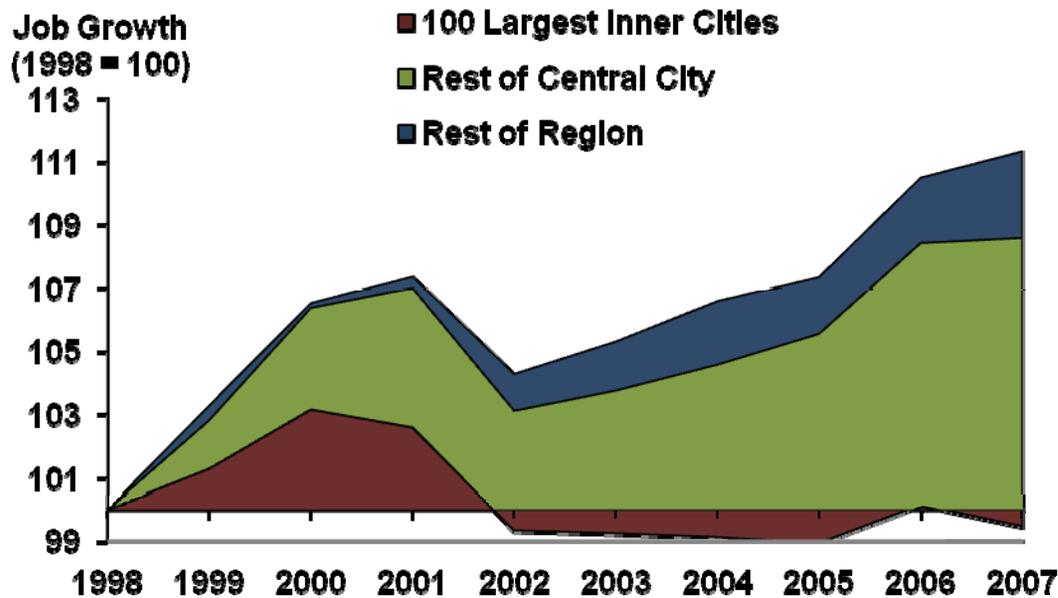
- Aggregating disparate small land tracts is challenging due to regulatory limitations such as zoning, and the complexity of negotiating with numerous distinct owners.
- Manufacturing legacy cities in the Midwest have significant tracts of land that can be developed.
- Site characteristics of heavy industry – access, shape, proximity to residential – are usually amendable to other industrial uses.
- Brownfield policy is a critical path item.



Over the past 15 years, there have been growing public and private efforts to leverage inner city assets through market-oriented approaches. There have been successes in some areas and challenges in others.

Overall inner city performance has significantly trailed regional performance.

➔ In ten years, the largest 100 inner cities created no net jobs, as a result of performance and not industry mix. However, growth for individual inner cities varied greatly during this period.

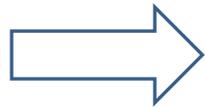


Source: State of the Inner City Economies (SICE) database; ICIC analysis.

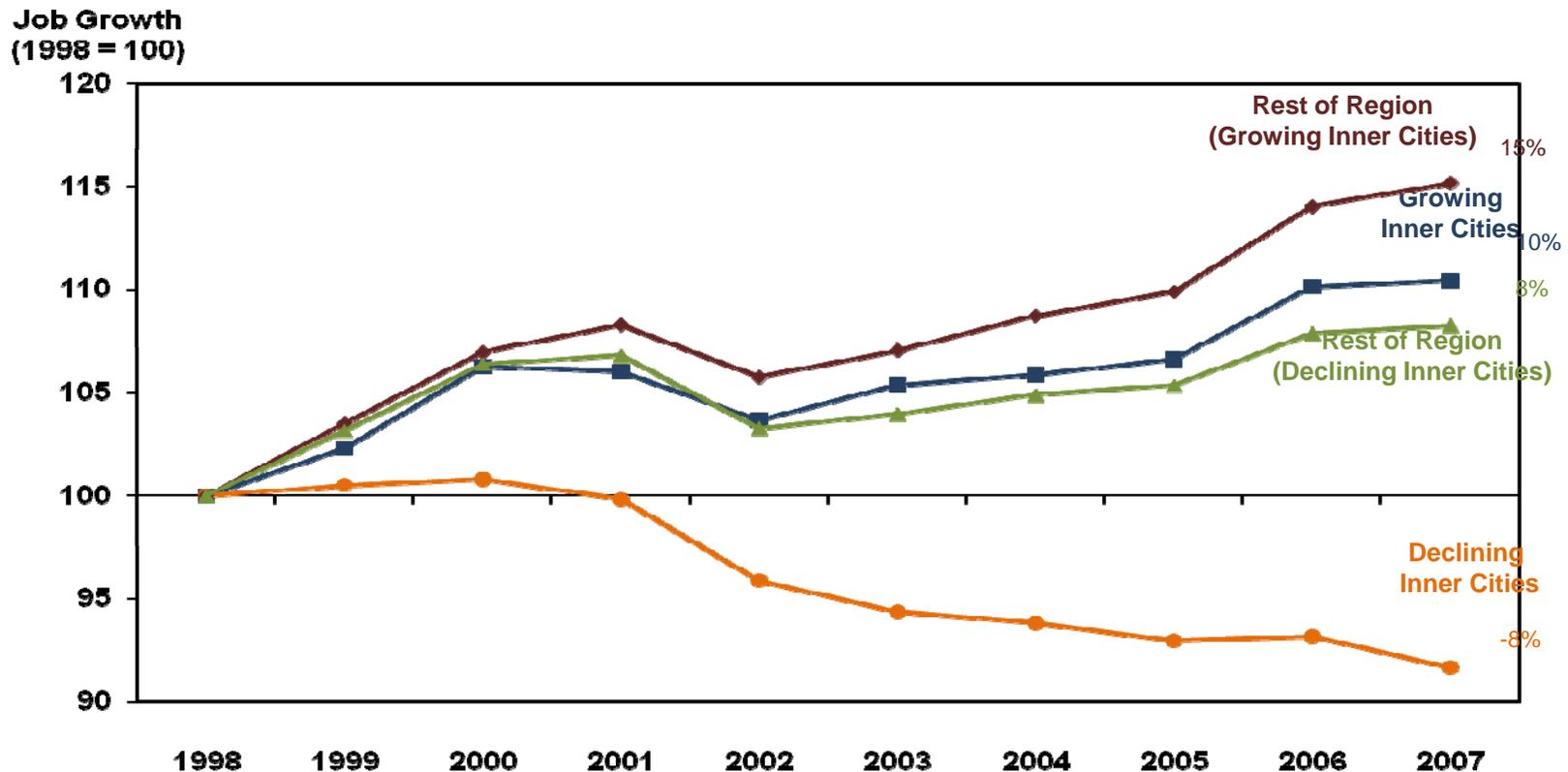
1998-2007

	Job Growth CAGR	Net Job Change
Rest of Region	1.2%	+ 6.7 million
Rest of Central City	0.9%	+ 1.4 million
Inner City	- 0.1%	- 50,000

Inner city economic performance varies, especially when comparing growing and declining inner cities.

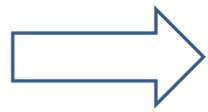


Growing inner cities experienced significant growth, while declining inner cities lost 8% of their job base. High growth companies, however, could be found across all categories.



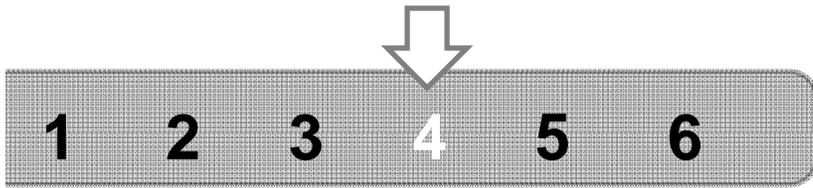
Source: State of the Inner City Economies (SICE) database; ICIC analysis. Data exclude New Orleans.

Exogenous factors account for a small portion of inner city performance.



The problems are local and less daunting than those associated with global economic trends or technological change.

Factor	Evidence
Regional economic performance	Regional economic performance accounts for less than 10% of inner city performance.
Globalization	Inner city economies are no more exposed to global competitive industries than anywhere else in the U.S.
Technological advancement	Inner cities perform reasonably well in emerging sectors including IT.



Inner city performance can be traced to challenges facing inner city firms and the business environment.

Key challenges include firm expertise, capital market weakness, and infrastructure quality.

Lack of business expertise among firms:

There is a weaker pipeline of successful business owners in inner cities.

Access to capital:

Fewer personal assets combined with good information on low income and inner city borrowers limits their capital access.

Poor quality infrastructure:

Older infrastructure and insufficient investment contributes to poor quality.

The federal government can play a key role in addressing these and related challenges at a local level; failure to do so will hamper market-based approaches at the city level.

Inner city entrepreneurs often have less experience and personal assets.

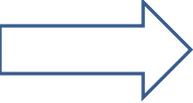
Minority business owners, particularly African Americans, are less likely to come from a family-business background where they learn business skills and industry expertise.

Research  *Lack of work experience from a family business negatively affects business outcomes.*

- Firms whose CEO's have a family history of business ownership are 28% larger in terms of revenue
- 60% of the 100 fastest-growing inner city firms in 2009 had a close family member who owned a business

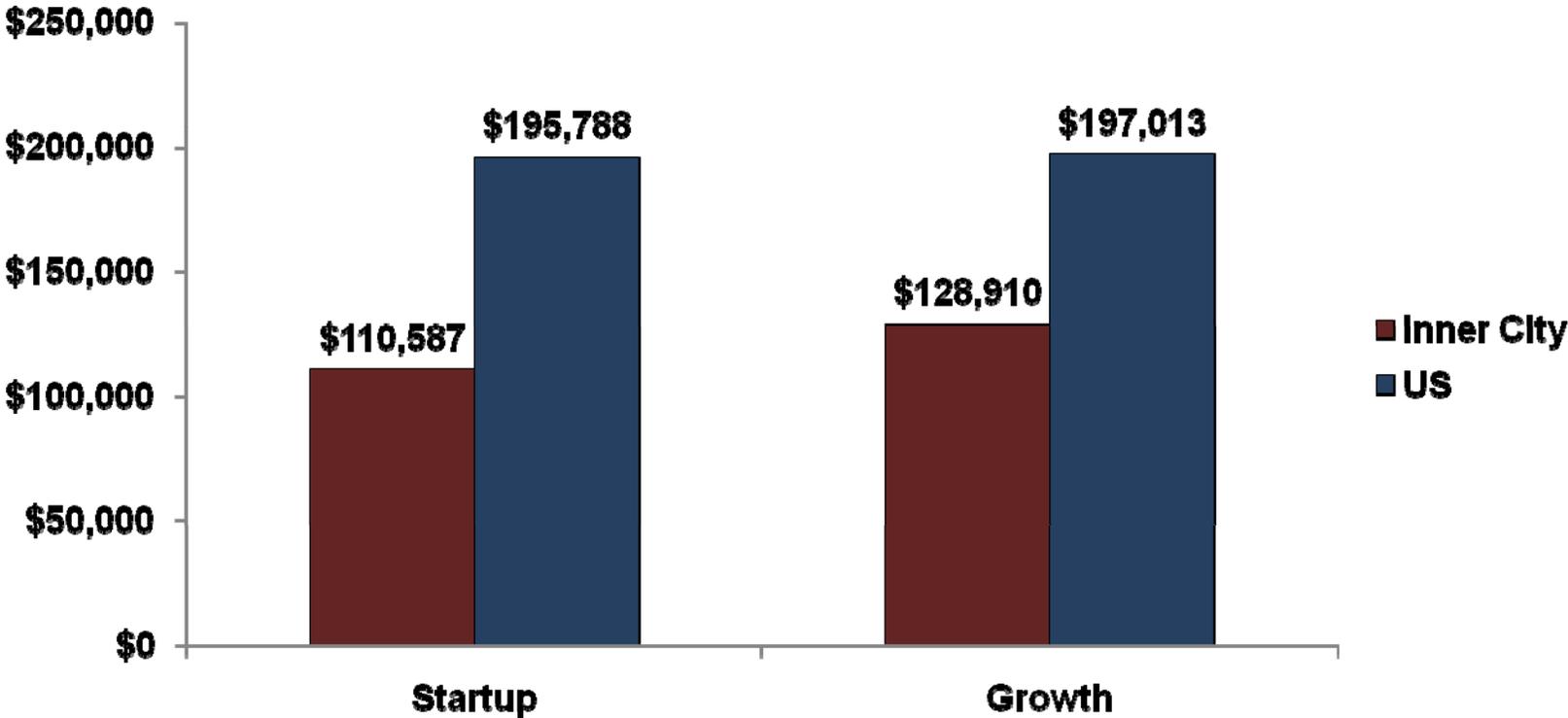
Disparities in net worth between whites and minorities may mean that the latter have lower levels of access to startup and growth capital.

Research  *These differences contribute to observed racial disparities in business outcomes.*

 Given these factors, inner business owners may need better advisory services.

Inner city businesses often face difficulty accessing capital, a problem exacerbated by current economic conditions.

Average Startup and Growth Capital (2004 – 2006)

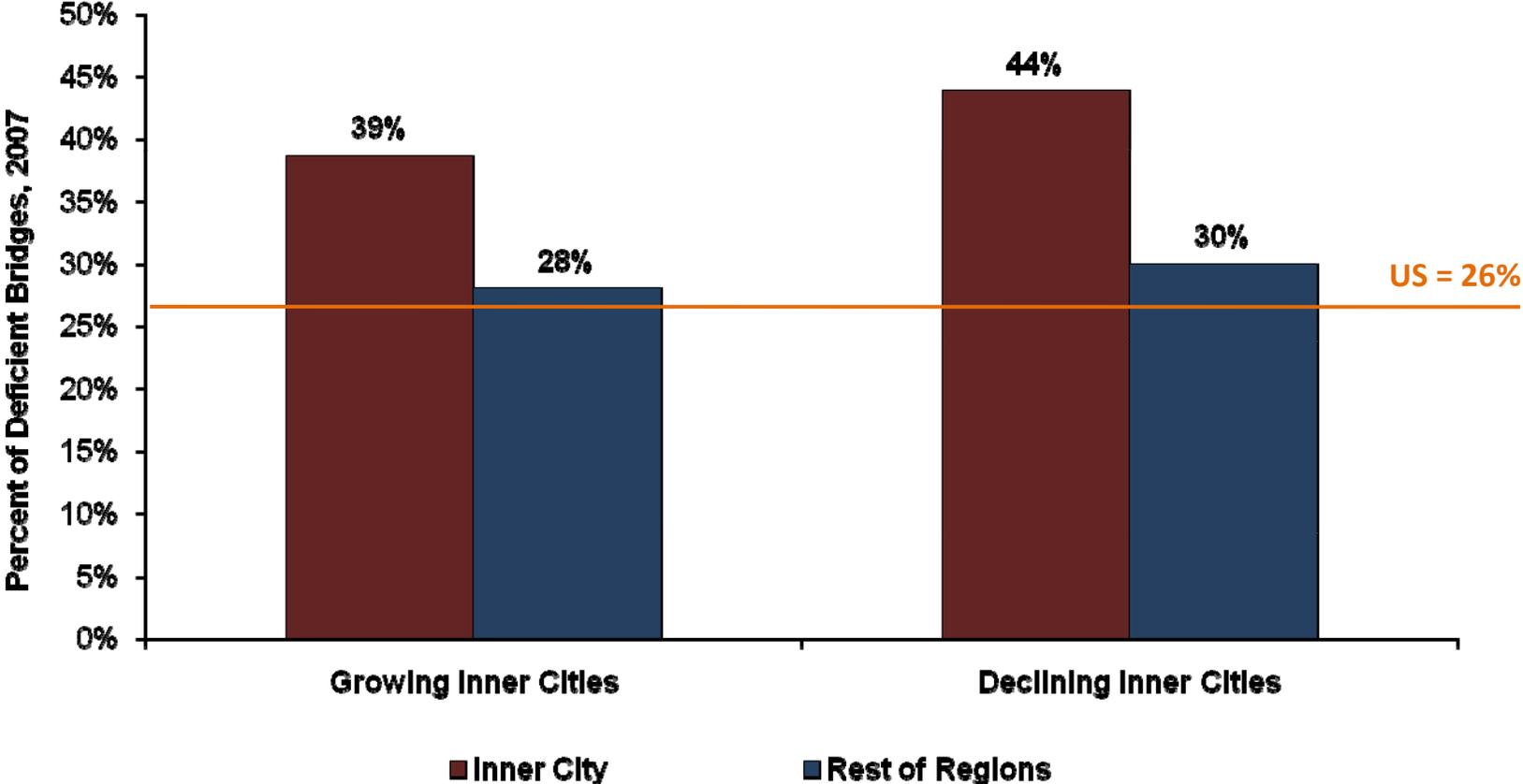


Note: Controlled for sector composition.



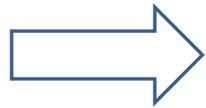
The quality of inner city infrastructure trails other areas of the country.

➔ Poor infrastructure quality, measured by examining deficient bridges, costs inner cities an estimated 150,000 to 250,000 jobs in key clusters like transportation and logistics.



Source: State of the Inner City Economies (SICE) database; ICIC analysis.

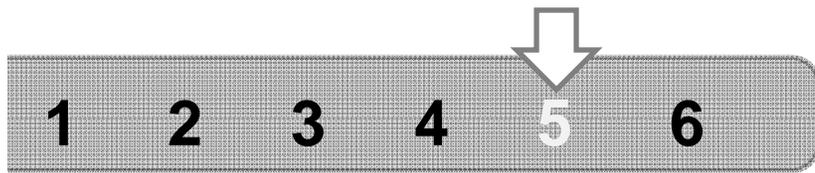
In addition to these obstacles, other serious challenges persist.



These factors can translate into higher costs of doing business.

Inner City Business Environment Challenges

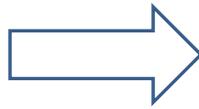
- Quality of the workforce
- Availability and quality of land
- Difficult regulatory environment
- Crime/perception of crime



Despite a strong rationale for federal government focus on inner city business development, existing policies and programs are not adequate.

Most existing federal policies and programs do not adequately address the challenges of inner city business development.

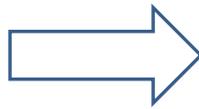
**Policy
Successes**



Stable **procurement**

Service **larger firms**

**Policy
Problems**



Lack of **focus and vision**

Minimal **scale**

Flawed program design/structure

Lack of relevant **data/information**

There are numerous federal business development programs, but they are fragmented and lack a unifying vision.

Drive demand for goods and services:

- SBA: 8(a), HUB Zones
- All agencies: Offices of Small and disadvantaged businesses

Increase availability of financing/capital:

- Treasury: CDFI Fund/NMTC
- SBA: 7(a), 504, SBIC
- CRA

Provide support and technical assistance:

- Commerce: Minority Business Development Agency, new Office of Innovation and Entrepreneurship
- SBA: Office of Entrepreneurial Development programs; Emerging 200, 8a, SBDC

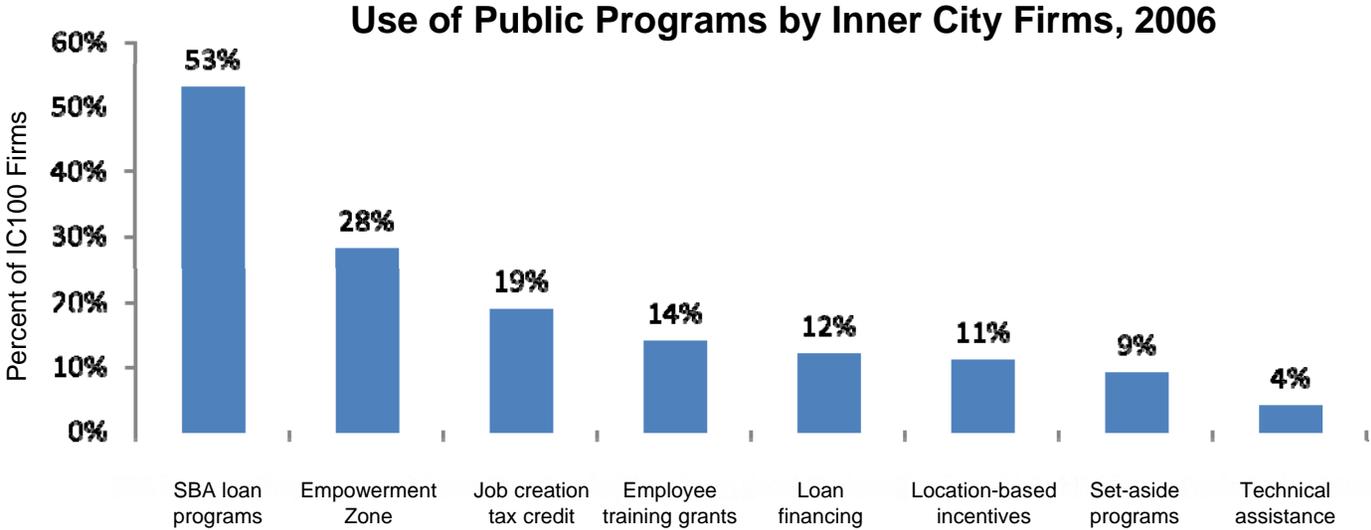
General urban economic development programs:

- HUD: CDBG, EZs/RCs
- EDA: various

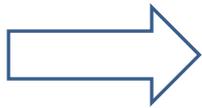
Plus dozens of workforce development, land/infrastructure, crime prevention, and other programs that affect the business environment

The federal government represents an important source of revenue and financing for inner city businesses.

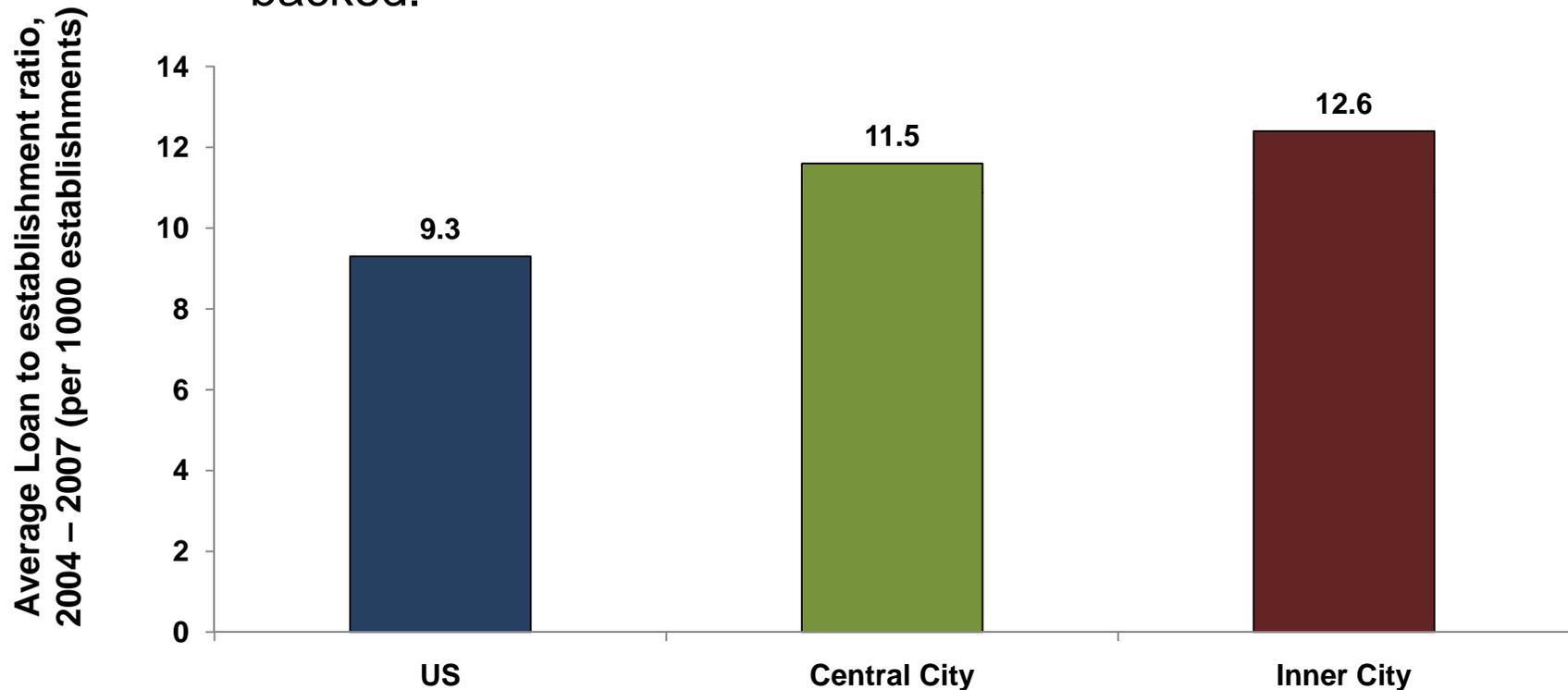
- Inner City firms identifying the government as their primary source of revenue have higher average revenues
- SBA loans, empowerment zone and job creation tax credits are the most often used public programs by Inner City 100 firms
- SBA loans represent an important source of financing for inner city firms that have achieved critical mass



SBA-backed loans are well represented in inner cities, but the absolute amount is minimal relative to the capital market failure in these areas.



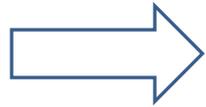
Only 2-3% of total small business loans (<\$1 million) are SBA backed.



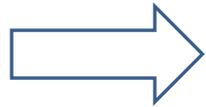
Note: Central City refers to all zip codes that are 99-100% in the central city. Inner City refers to all zip codes that are 99-100% in the central city and >0% in the inner city.

The design of federal place-based programs is such that they don't adequately address the needs of inner city businesses.

For instance:



New Market Tax Credits: While a successful program overall, 68% of credits are used for real estate projects versus 32% for business investment. NMTCs are also cyclical: the value of the credits falls when the economy slows.



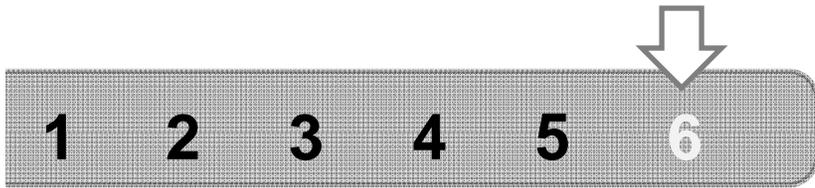
Empowerment Zone Program: Some aspects were innovative and positive, but the uptake of the incentives was generally low, and the program overall yielded generally inconclusive results.



HUBZone Program: According to GAO/SBA, the program is very diffuse. The number of qualified Zones increased from nearly 8,000 in 1999 to over 14,000 in 2006, and Zone economic characteristics vary widely.

Information on small businesses, consumer markets, and business lending in inner cities is limited or not easily accessible.

Type of Data	Primary Federal Government Sources	Primary Limitations - Examples
General data on business by industry and size	Economic Census; Zip Code Business Patterns; Business Dynamics Statistics; Longitudinal Employer Household Dynamics; Statistics of US Businesses	<ul style="list-style-type: none"> •Geographic units too large •Infrequent collection/reporting •Data categories too large for fine-grained analysis
Market data	US Decennial Census; ACS; Consumer Expenditure Survey	<ul style="list-style-type: none"> •Under-represents market demand •Geographic units (CE) too large
Data on federal funding flows	Consolidated Federal Funds Report; USAspending.gov; individual agencies and programs	<ul style="list-style-type: none"> •Geographic units too large •Interface not user friendly •Inconsistent; tedious to compile
Data on debt/equity financing	SBA data – various programs; CRA reported bank data	<ul style="list-style-type: none"> •No reporting on applications and denials •Reporting by loan size, not business size



Federal policy reform is needed to foster the growth of high performing businesses and ultimately help improve inner city economies.

Federal policy reform should be guided by a set of five principles.

- The federal government should **focus, leverage, and align** existing federal programs in support of a comparative advantage-based **approach** to inner city economic development.
- Federal **funding and effort** should be at a scale appropriate to the need.
- Federal focus should be on areas where there is the **greatest impact combined with clear justification for government involvement**: long-term correction of market failure (e.g., information), short-term compensation for market failure (e.g., capital markets), and equitable and rational provision of public goods (e.g., infrastructure investments).
- Federal policy and programs should recognize and be responsive to the **highly varied conditions of inner cities (and their regions)** across the country.
- Federal policy and programs should be **guided by better data** on the relevant unit of analysis and performance.

Federal policy should:



Focus on inner cities as distinct and important components of regional economies



Improve/increase **investment** to close capital gaps



Reveal the assets of inner cities through better data and information tools



Maximize the assets of inner cities, being attentive to their varied market conditions



Help drive **system** reform to maximize government performance at all levels



Broaden small business support to include training and advisory boards in addition to capital

Focus on inner cities as distinct and important components of regional economies.



Determine the Federal vision and desired outcomes for inner city economies

- The White House should bring together HUD, SBA, Treasury, Commerce, and other relevant agencies and offices to articulate the short-, mid-, and long term vision for inner cities, and develop outcome measures against which to benchmark program/policy success
- Agency efforts should better coordinate and align around the vision.



Convene a public-private-nonprofit sector consortium to promote learning, exchange, and policy advancement around inner cities

- The White House should use Federal convening power to host a series of meeting/events that bring community development entities, financial institutions, intermediaries, nonprofits, researchers, and government together around key issues facing inner cities

Improve and increase investment to close capital gaps



Establish an “innovation lab” within SBA or Treasury to develop innovative financing products and tools

- Would provide competitive funding for the development of new private sector products and tools focused on small business/community development finance
- Would focus ‘in house’ on developing new or improved federal programs focused on small business finance, with a focus on distressed communities and low-income borrowers (e.g., a national Capital Access Program, the next generation of financing vehicles)



Focus on coordinating and reforming existing technical assistance programs to deliver high quality, customized strategic planning and financial advice

- Could provide competitive grants/subsidies to private business support networks to provide strategic advice and services that help firms successfully access appropriate capital
- Could experiment with voucher programs covering part of cost for certain size/sector/place businesses to buy assistance from private sector providers/intermediaries



Explore the creation of a new and improved Empowerment Zone program

- Would coordinate effort among multiple federal agencies to provide resources in support of Zone strategic plans

- Would provide incentives to Zones to support their unique strategic assets and comparative advantages

Reveal the assets of inner cities through better data and information tools.



Create an interagency task force to improve data and information on inner cities:

- Would include the Census Bureau, Federal Financial Institutions Examination Council, BLS, SBA, and other relevant agencies
- Would focus on creating new and better federal data products and innovative tools that end users (cities, nonprofits, business groups, etc) want and can use



Create within HUD a ‘Metropolitan Markets Initiative’ to unveil the assets of underserved areas:

- Could facilitate private sector data consortiums around small business lending and urban markets (eg National Opinion Research Center (NORC) Data Enclave, see Milken)
- Would identify, help bring to scale, and disseminate innovations in data and information tools
- Would seed local efforts to develop creative models/tools designed to gather, analyze, and make available extensive, granular analysis on local market dynamics, including consumer demand, capital demand, clusters, etc.

Maximize the assets of inner cities, being attentive to their varied market conditions.



Launch a new initiative in HUD for land recycling in highly distressed cities

- Use a portion of HUD Challenge Grant funds to competitively award planning grants focused on vacant property management, zoning and land use reform, and property reuse in select distressed cities (2010)
- Provide funds for recipients of Year 1 Challenge Grants for plan implementation (for land banking, property maintenance, demolition, site improvements, code enforcement, etc.) (2011)



Focus federal infrastructure funding on maximizing economic benefit

- Target inner city infrastructure investments on the critical improvements needed to enhance the environment for business activity
- Measure the impact of investments against metrics of economic benefit



Leverage the anchor institutions in inner cities

- Create a division within HUD's Office of University Partnerships whose mission is to help leverage anchor institutions' economic assets, including purchasing, investment, hiring, business incubation, etc.; could provide seed funding for anchor efforts, as well loans and/or matching grants for state/local efforts
- Use the federal bully pulpit to encourage institutions receiving federal funding to develop locally-based procurement policies aimed at inner city and minority businesses

Help drive system reform to maximize government performance at all levels.



Alter the way the federal government does business to ensure that is customer- and outcome-driven

- Move beyond rule-driven administration to smarter, more flexible, demand-driven interaction with states and localities that focuses on achieving outcome-based targets
- Embrace partnerships, both intergovernmental and with the private-sector, to gather, scale, and disseminate innovative policies and practices



Work with states to ensure that local governments reform their own governance and regulatory systems to foster an environment conducive to economic growth

- Use both carrots and sticks to encourage cooperation – rather than competition - within metropolitan areas
 - Example: Cluster policy should acknowledge unique cluster strengths of inner city economies, and incent regional cluster activities to include inner city firms
- Help build the capacity of local governments to reform regulatory systems, such as antiquated permitting, zoning, and land use policies, that are a barrier to business attraction and growth



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