



United Way of Greater Los Angeles

Affordable Housing Initiative Fund

An Analysis of Investors' Needs and Priorities

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Abt Associates
6130 Executive Boulevard
Rockville, MD 20852

Abstract

United Way of Greater Los Angeles contracted Abt Associates to develop a tool to help potential investors decide whether the Affordable Housing Initiative (AHI) aligns with their impact investment priorities. To understand investor needs, Abt conducted an environmental scan to understand current practices in impact investing and interviewed investors identified by United Way. This report summarizes the findings and highlights investors' priorities and preferences.

Study Team

Nichole Fiore

Kimberly Burnett

Naganika Sanga

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1. Introduction

1.1 Affordable Housing Initiative Fund

There is increasing interest in impact investment¹ in affordable housing in the U.S. that can generate both social and financial impact. The United Way of Greater Los Angeles (United Way) launched the Affordable Housing Initiative Fund (AHI), an impact investment fund, in 2021 to support the development of affordable housing in California. AHI provides below-market capital to minority-led or -owned developers on flexible terms. In addition to eliminating barriers to reliable financing options, AHI aims to lower project costs by shortening the time developers usually spend in arranging the necessary capital to finance an affordable housing project.

According to the 2023 AHI Investor report, AHI's innovative financing model reduces the average development timeline by over a year and reduces the average development cost per unit from \$650,000 to under \$300,000. Envisioned as a \$300 million fund over three phases, AHI closed the Phase 1 Fund at \$62 million in June 2022. Phase 2 closed at \$112.25 million in October 2023. The final phase is expected to close in 2024.

United Way contracted Abt Associates to develop a tool to help potential investors decide whether AHI aligns with their impact investment priorities. To understand investor needs, we conducted an environmental scan to understand current practices in impact investing and interviewed investors identified by United Way. This report summarizes our findings and highlights investors' priorities and preferences.

1.2 Approach

In February 2023, the Abt team conducted an environmental scan of impact investing. This included reviewing the literature on impact investing trends, investor priorities and needs, and impact measurement tools and criteria, with a specific focus on affordable housing impact investments. During spring 2023, we interviewed investors identified by United Way and spoke with multiple impact investment and affordable housing experts. We also reviewed AHI documentation such as United Way's internal reports, presentations, and reference material on the AHI design and performance. Interviews with potential and current investors helped us understand investors' views, preferences, processes, and challenges in investing in affordable housing projects. This effort informed the development of the *Investor Alignment Tool*.

This report presents the findings from our investor interviews.

- The remainder of this section provides an overview of the interview sample, investors' organizational background, and the sectors they are currently prioritizing for their impact investments.
- The second section discusses investors' interest in the AHI Fund, the features they found most attractive, and the reasons why some investors did not invest in AHI. This section also discusses the challenges investors experience when investing in affordable housing.

¹ In this report we use the term "impact investing" to also encompass ESG (Environmental, Social, and Governance) investing. Although the terms can be used to mean different types of investing, in the context of AHI, we use 'impact investing' based on what we heard from the investors and our conversations with the United Way of Greater Los Angeles.

- The third section describes the processes investors use to select investments and the factors that influence their decisions.
- The final section highlights some ways the AHI Fund can be marketed to investors based on our findings.

1.3 Interview sample

We interviewed 15 current and potential AHI investors (see Exhibit 1). Most of the interviews (9) were with philanthropic entities. We also spoke with representatives from the financial services industry, investment firms, and major employers in the region. We interviewed investors identified by United Way. In discussing our findings, we anonymize our interviewees to protect the investors’ identities.

All interviewees provided insights into investors’ needs and challenges in affordable housing impact investing. Discussions with current AHI investors highlighted their experience with the fund and what AHI features were most attractive. Discussions with potential AHI investors provided insights into other investor priorities and needs.

All interviews were conducted virtually and semi-structured focusing on the following themes:

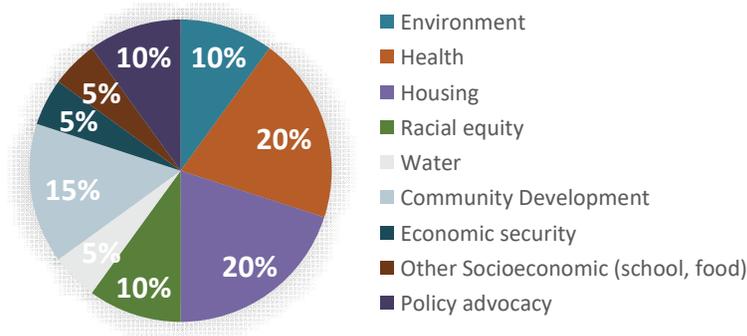
- Interest and motivation in AHI and other affordable housing investments.
- Overall impact investing goals, priorities, and expectation of returns – both financial and social.
- Due diligence practices in selecting investments.
- Tracking investment performance.

Most investors we interviewed invested in a variety of areas, including health, housing, community development, the environment, and racial equity.

Exhibit 1: Investor Interview Respondents

Type	Number
Financial services	2
Corporate foundation (embedded)	3
Philanthropy	6
Investment firm	2
Major employer in the region	2
Total (7 potential + 8 current investors)	15

Exhibit 2: Investment Areas by Interviewees



2. Investor Interest

2.1 Affordable Housing Initiative

We asked current and potential investors about what factors motivated their interest or reluctance to invest in AHI. Most AHI investors were interested in the fund because of United Way's sponsorship. Investors shared that United Way's reputation and decades of support for affordable housing and solutions to homelessness helped them trust the AHI Fund. Investors also reported that AHI's focus on responding to the Los Angeles affordable housing crisis was important to them because they were also strongly committed to improving affordable housing and homelessness in the region.

"The city (LA) is at the forefront of high housing costs. The building code, taxes, it's a recipe for homelessness. United Way has the opportunity to influence [change in policy]."

AHI Investor

Four AHI investors said that the involvement of large banks and financial entities in AHI appealed to them. Three said that they supported AHI's model and its potential impact on lowering housing production costs. They believed that AHI offered a quicker and easier alternative to building affordable housing than layering several governmental funding sources. Additionally, AHI investors who were new to investing in affordable housing believed that AHI would offer them learning opportunities.

"We are not housing experts... AHI helps us learn early, gets us into that environment of the housing world, talking, knowing who to talk to."

AHI Investor

Among potential investors who did not invest in AHI, three prominent reasons emerged.

1. Potential investors' mission did not align with AHI's mission. Four of the seven potential investors said they only selected investments that targeted systemic change. One potential investor further explained that although they appreciated AHI's focus on serving Black and minority-led developers, their organization was keen on understanding the ways in which structural racism affected communities of color and they specifically targeted their investments to close those economic gaps through systemic change.
2. Potential investors primarily invested in funds managed by experienced managers with a capital rating and considerable experience in bond financing, affordable housing finance, and market investments.
3. Potential investors believed that AHI's fund model did not align with their investment needs. Two potential investors said they preferred to invest directly in projects rather than a consolidated fund. Others believed that the fund size was a challenge—while two potential investors said the fund was too large to be managed effectively, two other potential investors thought the fund was too small to make any measurable impact. One potential investor also shared that the tax implications of the AHI, as currently structured, did not benefit individual investors with high net worth, who typically tend to prefer donor-advised fund platforms.

2.2 Reporting challenges

Both potential and current investors believed they did not have the in-house capacity to track and monitor their investments' performance. Investors also noted the challenges they encountered in determining their impact priorities and ways to quantify them.

Investors who have tried to formalize performance measurement internally shared that there were no current products that offered a reliable and convenient way to consolidate and measure social investment impacts. As a result, investors reported that they were completely reliant on fund managers and housing developers to identify metrics and report progress and performance. Most AHI investors said that they would like to receive more data on AHI performance. Investors said stories on fund performance would help them make a stronger case with their investment committees or board to invest in AHI.

2.3 Challenges in affordable housing impact investments

"Our return is impact, and we usually let folks measure their own impact. We don't want to say you have to build 40 housing units. You're in the local community, you tell us what are the important measures that we should think about when making the investment. So, the onus is on the borrower to tell what tracking and measuring they do."

AHI Potential Investor

Investors, both current and potential, mentioned a mix of challenges in affordable housing impact investing. While some challenges were specific to investments in housing, some were due to their organizational background and experience. Six investors said that it was hard to find 'shovel ready' projects that met all their requirements. Investors also felt that affordable housing projects tended to be more time-consuming and financially intensive compared to other investments. Having shovel-ready projects, investors shared, helped reduce the risks associated with time delays and increasing predevelopment costs.

Impact investing in affordable housing is relatively new.

Investors shared that the lack of necessary in-house capacity to manage impact investment portfolios and limited experience in affordable housing prevented them from engaging more deeply in such initiatives.

3. Investment Strategy

3.1 Due diligence practices and processes

Investors used a range of screening and due diligence practices to select investment opportunities. As discussed earlier, most of the interviewees we spoke with mentioned limited staff capacity as a major challenge. Most of the interviewees said they had a very small team of staff that managed their impact investing portfolio. Staff responsibilities include identifying opportunities, reviewing investment proposals, communicating with borrowers and fund managers, and presenting ideas to leadership.

“We do not have that level of sophistication to professionalize this work, we don't have the tools here. The vast majority of us do not have that capacity and most folks who are sitting in this role are not equipped to do that. They're not able to go into the deep dive.”

AHI Investor

Most investors had an internal investment committee that screened investment proposals. Two investors hired a consultant to perform detailed financial and legal checks before shortlisting potential opportunities for their investment committees. Two investors had fund managers who decided where and how much of the organization’s budget earmarked for impact investing to invest. Investors shared that because of limited staff capacity and the challenging process of quantifying social impact measures, they were not tracking their investments’ impact performance in a systematic manner.

3.2 Screening and prioritizing investment opportunities

Exhibit 3 provides the criteria investors use to select investment opportunities (ordered by priority). Most investors explained they would only invest in initiatives managed by organizations that were well-respected and had built a strong reputation through their impactful work, had equitable hiring and wage practices, had preferences for women and minority groups, and had strong leadership. In addition to fund managers’ and sponsors’ organizational profile, investors also mentioned that they examine the reputation and organizational record of other entities involved such as borrowers, their suppliers, community-based organizations, and financial institutions. Seven investors said that they preferred projects that involved community-led organizations in the design, development, and evaluation process.

Exhibit 3: Investor priorities for selecting investment opportunities.

High Priority
Reputable and experienced fund manager, borrowers
Replicable and scalable
Trusted and community-based intermediaries involved
Medium priority
Innovative and experimental initiative
Underserved by market
Short-term investment
Potential for policy and systems change
Potential for building investor reputation in housing sector
Low priority
Alignment with investor organizational values and priorities
Financial returns
Clear performance measures and outcomes

Investors prioritized investment opportunities that helped leverage more investments and expand the scale of an initiative. Given the novelty of AHI’s approach, investors believed that their early investments should impact standardizing the funding models, attracting more investments, and encouraging scaling the initiative.

Philanthropy making program-related investments in affordable housing initiatives felt strongly that their capital – usually offered at lower interest rates and for longer terms compared to market credit – should serve population that are underserved by market-rate housing. Philanthropy also prioritized initiatives that can attract government attention through their success and prompt policy change.

Five investors said they were interested in projects that supported deeply affordable housing; five said their focus was on projects serving disadvantaged communities. Another five investors said they wanted to support workforce housing; two of these five investors also supported projects that offered deep affordability. Four investors said they were keen on investing in new housing development and two mentioned that they did not want to support housing rehabilitation projects. For four investors, housing that provided ancillary health services was a priority. Investors were also interested in investments that

“It needs to be tangible, scalable, replicable, and measurable.”

AHI Potential Investor

“[We are interested in] investments focused on improving and racially diversifying investor manager class that is dominated by white men taking care of \$1 billion in assets.”

AHI Investor

directly supported Black and women-led developers. One investor specifically mentioned that they wanted to support funds that were managed by individuals representing minority groups.

Investors were also typically interested in supporting innovative and experimental initiatives that may involve high risk. When investing in high-risk ventures, investors preferred a short-term commitment.

Representatives from philanthropy mentioned that they screened investment opportunities to confirm they aligned with the foundation’s values and furthered the work they funded through their philanthropic grants. Some organizations shared that they prioritized initiatives that helped build a positive reputation.

Expectations of financial returns varied considerably among the types of investors we interviewed. Most philanthropy considered any positive return on investment, however negligible (0 to 3 percent), an acceptable financial return on their program-related investments. Since they were focusing on social impacts and trying to fill gaps left unserved and underserved by the market, they expected their financial returns to be lower than market rates. For-profit investors, however, said that they expected rates similar to market returns. It was clear that despite interest in supporting affordable housing, for-profit investors do not want to sacrifice financial returns for social impact.

“We’re looking at investments to make things faster, cheaper, and easier but also creating systems change, policy reform to enable production at a faster pace to combat the crisis.”

AHI Investor

When faced with competing funding applications, interviewees explained that foundations prefer to select investment opportunities that best align with their mission and values. Foundations also prefer investments that are carefully planned and managed and provide evidence of impact with reports, well-defined impact metrics, and impact stories.

4. Key Takeaways

AHI investors felt positive about their overall experience and potential investors were interested in the AHI fund and its mission. We believe AHI can encourage potential investors to invest in AHI and current investors to commit more funding. Drawing from interviews, below we highlight some ways AHI can position itself to attract more investors.

1. ***Continue to leverage United Way's reputation.*** Current investors were all primarily drawn to AHI due to United Way's reputation and experience in affordable housing. Prominently leveraging United Way's reputational capital in communication materials and drawing attention to its efforts addressing Los Angeles' housing and homelessness crisis can be attractive to investors.
2. ***Promote AHI's contribution in reducing development costs.*** Investors were all motivated by the scalability and replicability of AHI. Showing investors how the AHI model compares to other public affordable housing financing channels by quantifying time and cost savings (such as percentage cost reduction per unit, average time saved for arranging finance, construction, and occupation of units) and calculating the number of additional units these savings can finance can help investors envision how their investments can be scaled.
3. ***Partnerships with financial institutions.*** Investors shared that while United Way has a strong reputation in grant administration, they felt less assured about the financial impacts since fund management is a relatively new initiative for United Way. As United Way builds their experience through the success of AHI, visible participation from other financial institutions, including major banks or CDFIs, can help instill greater investor confidence.
4. ***Target investors who prioritize social impacts and are willing to accept less than market-rate financial returns.*** Addressing investor needs and targeting investors who are likely to prioritize social impacts over financial impacts can help AHI align better with investor goals. However, such organizations also look for deeper social impacts not only in terms of who the financed housing project serves, but also how the investment helps build organizational capacities and wealth for BIPOC developers. These investors sometimes channel their funds to initiatives that focus on local communities and community-based organizations designing and managing the project.
5. ***Build strong reporting and monitoring practices.*** One highly effective approach to capture investor interest would be for AHI to develop detailed reporting and performance tracking processes. Impact investors are likely to support investment opportunities where a fund manager tracks and reports investment performance regularly. Investors stated that it would be helpful if United Way could share the following details:
 - Periodic reports with financial and progress updates.
 - Organizational information on developers
 - Project status updates
 - Impact stories with details about the developer, the project built, and the people it serves.