HEALTHY NEIGHBORHOODS EQUITY FUND I LP

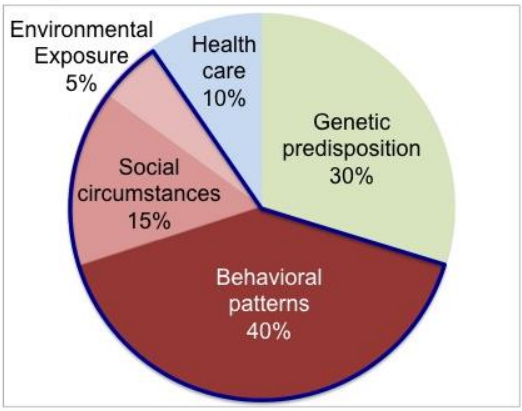
## Executive Summary

*Please note disclaimer at the end of this document.*

**National Context: Healthy Communities**

Health outcomes – traditionally a concern of public health practitioners and policy makers – are emerging as a critically important "fourth bottom line" for community investment. Several factors have contributed to this growing interest. First is the explosion of health care costs over the past decade which is creating a substantial drag on the U.S. economy and threatening to bankrupt public institutions. Second is the increasing scarcity of public funds to support affordable housing, transit, parks, and community facilities that constitute the building blocks of healthy communities. Finally, the alarming rise of obesity and chronic disease over the past decade has focused national attention on the built environment's role in shaping health outcomes. A 2007 New England Journal of Medicine article entitled "We Can Do Better - Improving the Health of the American People" identified behavior, environment and social circumstance as the largest determinants of premature death (together, these account for 60 percent). In contrast, genetics account for 30 percent, and health care only 10 percent[i].

**Proportional Contribution to Premature Death**




*Source: N Engl J Med. 2007 Sep 20; 357(12):1221-8, Figure 1.*

Consequently, even modest changes to the built environment, which in turn shape behavior and social circumstance, can drive significant changes in health outcomes. This is especially important for poor and working-class Americans who are far more likely to suffer from poor health. Direct health care costs for chronic disease, which account for 75 percent of health care spending[ii], are correlated with socio-economic factors, with diabetes and heart disease twice as prevalent among poor adults as among upper-middle-class Americans.[iii] Linking investments in community development with investments in health, especially in low and moderate-income neighborhoods, has the potential to improve lives, reduce health care expenditures, and build sustainable communities while creating new opportunities for socially responsible investment.

**The Opportunity for Transit-Oriented Development**

One of the most significant opportunities to impact community health at the neighborhood scale is through investments in transit-oriented development (TOD), defined as higher-density, mixed-use development within walking distance of transit. TOD projects are uniquely positioned to deliver a host of triple bottom line benefits, many relating to community health. A recent report from the Center for Transit-Oriented Development (CTOD) included the following benefits of TOD projects:

- Improved mobility options, so people can walk, bike and take transit, and access multiple destinations, including regional job markets, without a car;
- Increased transit ridership and reduced traffic congestion;
- Quality neighborhoods with a rich mix of housing, shopping and transportation choices;
- Revenue generation for both the private and public sectors;
- Improved affordability for households through reduced transportation costs;
- Reduced energy consumption, greenhouse gas emissions and air pollution; and



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- Health benefits resulting from reduced auto dependence and healthier lifestyles. [iv]

**Local Context**

Massachusetts is characterized by a strong regional economy and real estate market, but is also marked by pockets of intense poverty and a high degree of racial and income segregation. Since 1990, the number of poor people in Massachusetts has grown by one-fifth, while the number of Massachusetts residents living in high-poverty neighborhoods has increased by nearly one-third.[v] Furthermore, over the last decade, the number of households in Massachusetts spending more than 35 percent of their income on housing has gone up by 66 percent. This has become an urgent economic development issue, threatening the state's competitiveness as growing numbers of individuals and families are unable to afford the combined costs of housing and transportation.

Significant challenges have also emerged in population health. In spite of Greater Boston's status as a world leader in health services and research, the state has seen an alarming rise in obesity and chronic disease over the past decade. The Massachusetts Department of Public Health (MDPH) estimates that $1.82 billion per year in medical expenses in the state are directly attributable to adult obesity, a known correlate with hypertension, dyslipidemia, type 2 diabetes, coronary heart disease, stroke, osteoarthritis, respiratory problems, and certain cancers, including endometrial, breast, and colon cancer. These impacts are especially acute in low-income neighborhoods and communities of color, as evidenced by a 2007 study by the Commonwealth of Massachusetts Executive Office of Health and Human Services highlighting the disproportionately high rates of obesity, hypertension, diabetes, and asthma among Blacks and Hispanics.


Residents of lower-income neighborhoods also face myriad stresses related to economic security, public safety, transportation, food access, and environmental exposure, all of which can exacerbate chronic health conditions. **These health disparities, driven in part by neighborhood conditions, have resulted in a shocking 33.5-year difference in life expectancy at birth between residents of two nearby census tracts in Boston.** A distance of a few miles between neighborhoods can amount to decades of lost life.

In addition to economic and health concerns, Massachusetts faces significant environmental challenges related to greenhouse gas emissions (GHGs). The transportation sector represented 38 percent of total emissions in 2009, the largest single contributor to GHGs. Of particular concern is the rapid growth in transportation-related emissions in Massachusetts over the past two decades; from 1990 to 2000, these emissions rose by 11 percent, and from 2000 to 2005 they rose an additional 6 percent. Although the growth rate has fallen slightly since 2008, transportation is still the biggest GHG culprit. For these reasons, the future environmental health of the region will be determined in large part by the extent to which new development occurs in neighborhoods with access to transit and services that allow people to walk more and drive less.

All of these trends point to the growing importance of walkable, mixed-use, transit-oriented neighborhoods as a centerpiece of any future growth strategy for the state. Massachusetts is fortunate to have a strong network of Community Development Corporations, for-profit developers, a progressive state government, and a well-utilized transit system. A consensus is also emerging at the state level regarding the importance of Transit-Oriented Development. New private-sector financing tools, alongside public policy and regulatory action, will be necessary to accelerate TOD and healthy neighborhood projects at the pace that is required to meet regional planning goals and address the interwoven challenges of economic development, public health, and GHG emissions reduction.

*One-third of all assets in the US today are real estate, "and there is a huge pent-up demand for walkable urbanism… All of the growth over the next generation, if we give the market what [people] want, will be walkable urbanism."*

Christopher Leinberger, President of LOCUS: Responsible Real Estate Developers and Investors. Nonresident Senior Fellow at Brookings Institution.

**Goals and Objectives**

In response to these challenges, the Conservation Law Foundation (CLF) and the Massachusetts Housing Investment Corporation (MHIC) are working in collaboration with public and private partners to accomplish the following goals:

- Attract new sources of private equity to support moderately priced and market-rate housing, local job creation, commercial development, and healthy, walkable, mixed-use neighborhoods;
- Align equity investments with other sources of funds, including state housing, economic development, and infrastructure dollars, in order to catalyze and accelerate the development of high-impact TOD projects along key transportation corridors.

Done properly, the development of mixed uses and walkable neighborhoods around transit nodes will bring long-term transformative impacts. However, the project debt financing will be based on demonstrated value – that is, pre-transformation. It is, therefore, the goal of the Healthy Neighborhoods Equity Fund (HNEF) to tap that future value and bring it forward to help make financing of these transformative projects feasible.

**Transformative Value: The Role of Private Equity**

A 2011 study commissioned by the Metropolitan Area Planning Council (MAPC) and the Metro Boston Sustainable Communities Consortium found that the lack of patient, low-cost equity for moderate-income and market-rate housing as well as retail/commercial and industrial space is one of the most significant challenges to financing mixed-use, mixed-income TOD projects in Massachusetts. Simply stated, the markets in most locations, particularly lower-income neighborhoods that stand to benefit the most from this type of development, are not strong enough (or have not yet proven themselves strong enough) to support these uses at scale. Available subsidies are limited and highly competitive, and most non-profit developers do not have sufficient equity to self-fund projects of this scale. Private developers, meanwhile, often view projects in these locations as too risky. Further compounding this issue, underwriters are unwilling to finance future value, thus underwritten rents are limited by the rents in the surrounding neighborhood. This is a particular challenge for commercial projects where debt levels going in will be based on the strength of pre-leasing. Over time, real estate values in the neighborhood have strong potential to grow, but project sponsors have no way to monetize this long-term growth.

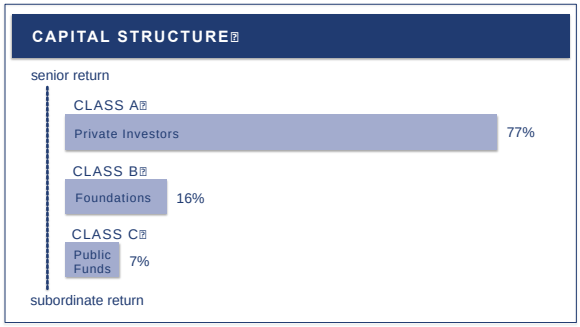
Therefore, our Quadruple Bottom Line (QBL) HNEF will provide new patient capital from private equity, philanthropic, and high net worth impact investors, to enable larger-scale TOD projects to move forward that would not otherwise be feasible in a transitional real estate market. HNEF will also leverage as much as 4:1 other sources of public and private financing, including both conventional debt and tax credit equity, and provide greater assurance to lenders and public agencies that the projects are worthy of investment.


**Pro-forma Expectations**

HNEF is designed to provide gap financing for transformative transit-oriented development projects that promote community, environmental and health improvements. HNEF equity can finance 5 to 25 percent of total development costs. This range reflects the differing ability of project sponsors to: (a) obtain public subsidies or philanthropic resources to fund the project; and/or (b) invest their own equity. It also reflects projects' varying degree of upside potential. Investments will typically be made at construction loan closing, and are expected to have a term of up to 10 years. HNEF will take an ownership position in the project partnership as a limited partner or investor member. Projects are expected to deliver a target IRR of 10% over the life of the investment, including annual cash distributions and back-end proceeds. Project sponsors must have a defined plan to take out HNEF equity at the end of the investment period. HNEF is not designed to finance permanently restricted affordable housing, but rather to finance mixed-use office, retail, and moderate- and market-rate housing where there is anticipated increase in value from future rent increases and/or neighborhood transformation.

**Fund Management: A Compelling Partnership**

MHIC has 25 years of experience investing in low-income neighborhoods through multiple investment funds, and CLF has decades of experience working for healthier communities and environmental justice across New England. MHIC will manage the fund, and undertake project due diligence, while CLF will review pipeline projects for conformance with HNEF's healthy community goals, and carry out long term monitoring of health outcome metrics. MHIC's HNEF Committee will review recommendations jointly made by MHIC and CLF and will recommend the final selection of investments to the MHIC Board of Directors. MHIC will be responsible for closing and managing approved investments. MHIC's asset management department (currently with over $1.2 billion in assets under management) will work to ensure long-term success of the investments.




**Fund Structure and Capitalization**

HNEF has a blended capital stack that enables the fund to make transformative impact investments while meeting investors' return expectations. Public funds, which do not have any return requirements, make up 7% of the estimated fund size (the Class C Investors). Program-related investments and investments by MHIC backed by guarantees from foundations make up 16% of the estimated fund size, and have modest return expectations (the Class B Investors). Socially motivated economic investors make up the balance of the fund as Class A Investors, and



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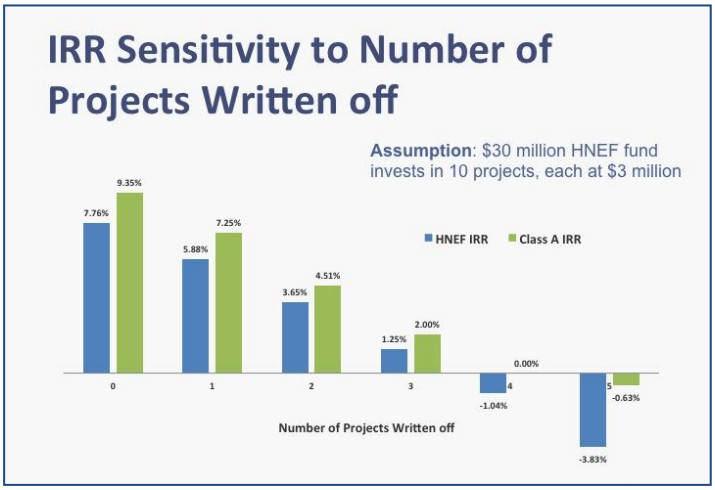
have a higher targeted return and upside potential.

**Managing Downside Risk**

HNEF will only invest in projects with strong community and public sector support. Leverage will be limited to no greater than 75 percent. In addition, as demonstrated in the graph to the right, the subordinate Class B & C capital provide "credit enhancement" to reduce risk to Class A investors (see sensitivity analysis).




**Evaluating Impact**

HNEF is based on a socially responsible investment (SRI) model that takes into consideration the community, environmental, and health benefits of a potential project as well as the financial risks and returns. The fund's approach to measuring these impacts has been shaped by a Health Impact Assessment (HIA) conducted by MDPH and the MAPC for three sample projects in Roxbury, Massachusetts. To assess the potential impact of TOD projects on neighborhood health, the HIA identified twelve focus areas. According to the HIA report, "these focus areas, called pathways, can affect health outcomes and chronic conditions such as obesity, stress, mental health, cardiovascular disease, respiratory disease, injuries, and premature mortality. Therefore, this HIA as a resource for the HNEF, summarizes major findings, isolates relevant health-related metrics, provides methodologies for how to model or predict future health impacts from land-use decisions, and offers specific recommendations to improve each health determinant through TOD development. By conducting an analysis on three proposed TOD projects cumulatively, this HIA found that, based on several assumptions, these TOD projects would have an overall positive public health impact."


*Health Impact Assessment: Pathways Impacting Health Outcomes and Chronic Conditions*

**HNEF Project Review and Rating System**

Using the HIA findings and recommendations as a foundation, HNEF will seek to invest in neighborhoods that are in the early to mid-stages of transformational change, and where an investment from the fund can help catalyze and accelerate that change. HNEF sponsors will seek to partner with projects that implement a community vision, capitalize on the investments already made by other sources, and demonstrate clear potential to advanced regional equity and reduce health disparities. As part of the evaluation process, CLF will use a detailed scorecard



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that integrates more than 50 quantitative and qualitative measures on neighborhood demographics, community conditions, health outcomes, and project characteristics to evaluate the need and opportunity for healthy development and quantify the expected impact of the project. The scorecard will also provide baseline data for monitoring a range of project outcomes over the life of the investment. Projects under consideration for HNEF investment will receive an overall HealthScore rating which will be presented to the HNEF Committee alongside the financial underwriting and real estate review. To receive an HNEF investment, projects must have a minimum HealthScore rating in addition to financial strength.

One of HNEF's long-term goals is to grow our understanding of the relationship between the built environment and health. To advance this goal, CLF, with support from the Robert Wood Johnson Foundation, is conducting a baseline evaluation to understand better the impact of fund investments on neighborhood conditions and health outcomes. This evaluation, which will be the basis for a longitudinal research study, is being conducted in partnership with the Harvard School of Public Health Center for Population and Development Studies, MDPH, MAPC, community-based organizations, and other local and national experts. This independently-funded research project will allow HNEF's sponsors to focus on their core responsibilities to investors while generating significant new data on health and neighborhood change that will be of interest to HNEF and a wider audience. We anticipate that the research effort will track neighborhood changes across multiple domains over a five- to ten-year period, consistent with the timeframe for equity returns to HNEF investors. These domains include economic, social and behavioral, environmental, and health outcome indicators, some of which will also be tracked for purposes of HNEF monitoring. Taken together, these indicators can help to predict and track neighborhood change over time and provide important insights about the connections between the built environment and health outcomes.

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[i] Schroeder S. We Can Do Better: Improving the Health of the American People. N Engl J Med 2007; 357:1221-1228.
[ii] Anderson G. Chronic conditions: making the case for ongoing care. Baltimore (MD): John Hopkins University; 2004.
[iii] Berkman L., Kawachi I., editors. Social epidemiology. 1st ed. New York (NY): Oxford University Press, 2000.
[iv] Fogarty N & Austin M. "Rails to Real Estate: Development Patterns Along Three New Transit Lines" Center for Transit-Oriented Development; March 2011.
[v] Geographic Segregation: the Role of Income Inequality. Forman and Koch, Communities and Banking. Federal Reserve Bank of Boston, Fall 2012.