Small Business Capital: A Place-Based Approach

Local governments and place-based philanthropy partnerships are unlocking opportunities and paving the way for equitable access to capital for small businesses.

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Accelerator for America and the International Economic Development Council are excited to present the first segment in a two-part series exploring the needs and opportunities to drive more equitable entrepreneurship and small business growth in communities across the U.S. This first piece addresses equitable capital access, and the second will delve into the other critical elements of the entrepreneurial and small business ecosystem that are necessary to foster inclusive growth. Both parts of the series will focus on the role that mayors, local governments, and place-based philanthropies can play in addressing gaps and creating more equitable opportunities in their communities.

The Longstanding Challenge

Mayors and local economic and community development leaders are keenly aware of the critical role that small businesses play in the economies of their cities and regions. Small businesses employ nearly half of the U.S. private sector workforce and have generated two-thirds of new jobs created since 1995.[1] Small business ownership can play an important role in individual, family, and community wealth building, with self-employed individuals being wealthier than non-self-employed people, and business equity being second only to a primary residence as a share of non-financial assets.[2]

The U.S. Small Business Administration found that small businesses are responsible for generating 44% of all U.S. economic activity.[3] Every dollar spent at a small business creates an additional 50 cents in local business activity as a result of employee spending and businesses purchasing local goods and services.[4] Local leaders see the direct impact of small business growth (or decline) on their local tax base and the availability of public resources to provide critical services and enhance the quality of life for all residents.

Cities and communities across the U.S. have extreme and long-standing racial and ethnic gaps in small business ownership. Despite representing 18.7% and 12.4% of the U.S. population as of 2020, Hispanic or Latino(a)s and African Americans own 7% and 3% of all businesses, respectively. Black-owned firms accounted for just 1% of American small business gross revenue, and Hispanic-owned businesses accounted for just 3% of such gross

[1] U.S. Small Business Administration Office of Advocacy. "Frequently Asked Questions." March 2023.
[2] Brian Headd, U.S. Small Business Administration Office of Advocacy. "Small Business Facts: The Importance of Business Ownership to Wealth." August 2021.
[3] U.S. Small Business Administration Office of Advocacy. "Small Businesses Generate 44 Percent of U.S. Economic Activity." January 30, 2019.
[4] American Express. "Another Reason to Shop Small® on Small Business Saturday®: Approximately 67 Cents of Every Dollar Spent at a Small Business Remains in the Local Community." November 13, 2018.

revenues in 2020.[5] Researchers for Brookings Metro calculated that there would be nearly 800,000 more Black-owned businesses if the rate of Black business ownership of employer firms was equivalent to population share.[6] Further, according to the McKinsey Institute for Black Economic Mobility research, an additional $200 billion in recurring direct revenues would be generated if existing Black-owned businesses reached revenue parity with their White-owned industry counterparts.[7]

The disparities – and the economic opportunity if these gaps are addressed – are stark at the local level. A 2023 analysis by Lending Tree evaluated the top 50 metropolitan regions in the U.S., finding that Atlanta, GA, had the highest percentage of Black-owned businesses with employees at 7.4%, with the Black population comprising more than a third of metro residents.[8] In Philadelphia, PA, an Equitable Entrepreneurial Ecosystem Assessment report noted that Black and Latino(a) residents account for more than half of the city's population, but own less than 10% of local small businesses with employees.[9] In Tucson, AZ, the city's population is nearly 45% Hispanic, but the Tucson region ranks 79th among the top 100 US metros for Latino business ownership, with three Latino-owned firms for every 1,000 Latino Tucson residents.[10]

In the city of St. Louis, White-employed residents are 36% more likely to own businesses than Black-employed residents.[11] According to the same Brookings report mentioned earlier, if the number of Black-owned employer firms in the St. Louis metropolitan region reached parity with its Black population share and the average employment size for all businesses, then there would be more than 9,400 additional Black businesses and nearly 300,000 additional jobs in the metro area. The report also found that eliminating the employee pay gap between

[5] Rebecca Lepert, Pew Research Center. "A look at Black-owned businesses in the U.S." February 21, 2023.
[6] Andre M. Perry, Regina Seo, Anthony Barr, Carl Romer, Kristen Broady; Brookings Institution. "Black-owned businesses in U.S. cities: The challenges, solutions, and opportunities for prosperity." February 14, 2022.
[7]McKinsey Institute for Black Economic Mobility. "Building supportive ecosystems for Black-owned US businesses." October 29, 2020.
[8] Maggie Davis, LendingTree. "Atlanta is Nation's Hub for Black-Owned Businesses." February 6, 2023.
[9] Next Street, Urbane Development, Econsult, and SourceLink for the United Way of Greater Philadelphia and Southern New Jersey, the City of Philadelphia, and PIDC. "Philadelphia Equitable Entrepreneurship Ecosystem Assessment and Strategy." May 2021.
[10] Ian O'Grady. "Tucson IDA Capital Landscape + Opportunities." September 15, 2022.
[11] City of St. Louis, MO. "Business Ownership."

Black businesses and all businesses would increase the total pay of St. Louis metro area employees of Black businesses by nearly $600 million.[12]

While multiple and intersecting reasons exist for this gap in small business ownership, access to capital is a critical obstacle. According to a 2023 report by the Federal Reserve System, new businesses owned by people of color that had or planned to have employees were denied the full amount of credit they applied for 53% of the time. In contrast, similar White-owned startups were only denied 27% of the time.[13] This is in line with the findings of a 2021 research report by Rob Fairlie, one of the leading researchers on firms of color, and his research partners. They found that Black businesses face disparities compared to their White counterparts, reporting, "The persistent difference in funding is driven primarily by differences in the amount of bank loans and other bank credit products, which in turn are not substituted by other sources of capital."[14]

Many mayors and local leaders have recognized that they must focus on growing their cities' economies in ways that directly address these disparities, including meeting the capital needs of entrepreneurs of color. This approach has both the direct benefit of generating more equitable local wealth and employment growth, while also having the indirect benefit of increasing the local tax base for the benefit of all residents. In the absence of a growing, inclusive local economy that generates sufficient resources to meet community needs, place-based philanthropies are often called upon to fill the void by supporting health, human services, food access, and other critical resources. As noted by contributor Dr. Dell Gines in the Federal Reserve Bank of Kansas City *Funder's Guide*, "Because of the many needs in low- and moderate-income communities, many funders consistently make choices between supporting the immediate needs of a community, such as food pantries and shelters, and providing support to help create healthy and economically viable communities over the long term…To improve the economic health and viability of communities over the long run, greater economic growth must occur within these communities. By strengthening local economic conditions, the need for funds that deal with immediate community needs decreases over time as the community is able to better sustain itself…An improved local economy also creates a stronger tax base and advances the health of the broad regional and state economy."[15]

How can we create a virtuous cycle wherein place-based philanthropy can support business growth that, in turn, supports community growth? How can place-based philanthropy pivot from often being the triage for community needs to the catalyst for community wealth?

[12] Andre M. Perry, Regina Seo, Anthony Barr, Carl Romer, Kristen Broady; Brookings Institution. "Black-owned businesses in U.S. cities: The challenges, solutions, and opportunities for prosperity." February 14, 2022.
[13] Lucas Misera, Federal Reserve Bank of Cleveland and Emily Ryder Perlmeter, Federal Reserve Bank of Dallas. "2023 Report on Startup Firms Owned by People of Color: Findings from the 2022 Small Business Credit Survey." June 2023.
[14] Fairlie, Robert, Alicia Robb, and David T. Robinson. "Black and white: Access to capital among minority-owned start-ups." *Management Science* 68.4 (2022): 2377-2400.
[15] The Federal Reserve Bank of Kansas City "Funder's Guide: A Guide to Funding Small Business Development Organizations."

The Urgent Opportunity

While there is a clear case for investing locally in equitable small business growth and the flexible capital needed to support it, this has not emerged consistently as a top funding area for place-based philanthropy. According to insights from LOCUS, a national nonprofit consultancy and mission-driven investment advisory firm, some of the common reasons for this include: fairly narrow interpretations of philanthropic mission statements or founding charters, historic focus on the social and human services sectors rather than the community economic development domain, misconceptions that providing resources to small businesses is not a charitable activity, and/or concerns about competition for resources with the nonprofit community.[16]

This dynamic began to shift during the COVID pandemic, as both the economic and social impact of a thriving small business community became very clear once it was fundamentally threatened. The disparate impacts of COVID on Black- and Brown-owned businesses, as well as the broader racial justice reckoning that took place simultaneously, shifted focus to bringing a racial equity lens to small business and entrepreneurial support in cities across the U.S.

A survey by Exponent Philanthropy and Peak Grantmaking found that nearly 80% of philanthropies followed different approaches to funding in response to COVID-19, with more than 40% making grants outside of their normal portfolios; this includes grants supporting small businesses and their employees (14%). The report also noted that nearly half of respondents had contributed to a local COVID-19 relief fund and/or created their own.[17]We must continue advancing these funding avenues to build on the momentum for local government and philanthropy partnerships to move beyond pandemic relief efforts and toward supporting inclusive small business growth. If this progress isn't maintained, the likelihood of slipping back toward the low, pre-pandemic levels of engagement in the sector grows exponentially.

[16] Sydney England, LOCUS Assistant Vice President, Local Investment Strategy.
[17] Exponent Philanthropy and Peak Grantmaking. "COVID 19: How Have Funders Changed Their Approach & What Will Stick?" 2020.

This opportunity takes on even greater urgency in the context of the major industrial transition that the U.S. is undergoing, as outlined in recent research by the Nowak Metro Finance Lab of Drexel University. Market dynamics, rising global tensions, and large-scale federal investments are simultaneously driving three major economic shifts across the country: (1) reshoring, (2) remilitarization, and (3) decarbonization. Minority-owned firms' participation in the industry sectors that will benefit from these dynamics is strikingly low.[18]

The gap is especially stark for Black-owned businesses, which account for 1% or less of all employer firms in construction, manufacturing, and utilities despite Black Americans representing 13.6% of the U.S. population. In manufacturing, 4% of employer firms are Latino-owned, while nearly 19% of the U.S. population identifies as Hispanic or Latino/a.[19] The U.S. Small Business Administration reported that federal contracting with Black- and Latino/a-owned small businesses was less than 4% in 2021.[20]

There have been nearly $4 trillion in new federal appropriations since 2021, but not everyone or everywhere is positioned to benefit. These investments represent an unprecedented opportunity for underrepresented entrepreneurs and communities. However, without addressing the larger-scale capital needs these industries require or implementing intentional strategies to support existing minority-owned firm expansion, new business formation, and access to contract opportunities at all levels of these supply chains, these communities will be passed over once again.

While the federal government and the private sector (including commercial banks, private equity, and venture capital) must urgently address these gaps, city leaders and place-based philanthropy partners must also play an important role in shaping future outcomes through intentional action and investments. The current landscape encompasses efforts to drive innovation in place-based philanthropy, post-pandemic shifts, a much greater and long overdue emphasis on racial equity, and the opportunity to leverage philanthropic funding with the massive new infusion of federal investment into infrastructure, clean energy, and American communities. Combined, this presents a unique opportunity to bring city leaders and place-based philanthropies into closer alignment on growing local economies and enhancing the quality of life for all residents and communities through equitable small business development and capital access.

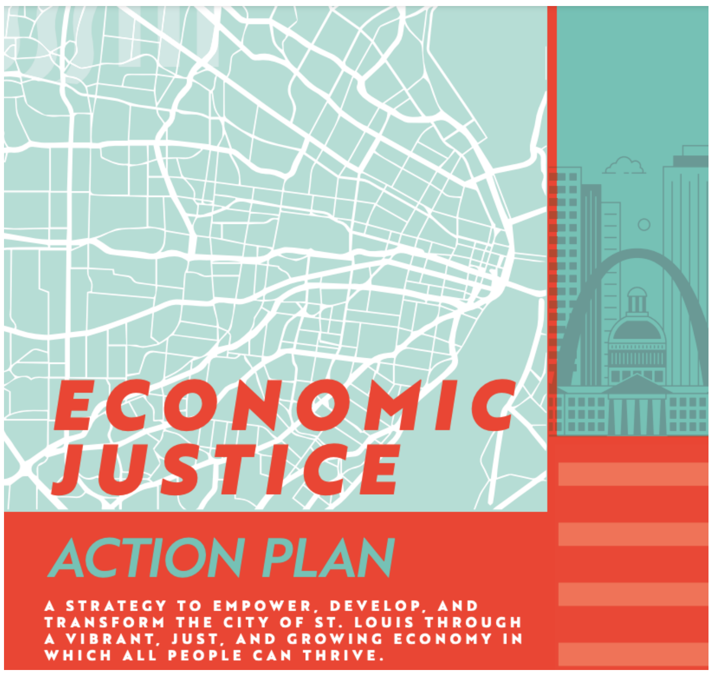
Role of Mayors and Local Leaders

As the chief executives of their cities, mayors have a unique role and opportunity to offer bold visions for equitable small business growth in their communities and to use their special convening power to bring together the city or region's philanthropic and capital ecosystem to better meet the needs of entrepreneurs. Local leaders can also strategically invest public dollars to help meet critical gaps in the market. Given that public funding at the

[18] Bruce Katz, Co-Founder and Director, Nowak Metro Finance Lab, Drexel University. "Everything Everywhere All At Once." April 2023.
[19] Source: U.S. Census Annual Business Survey 2018, Characteristics of Businesses and July 2022 U.S. Census Bureau data.
[20] The White House. "The Benefits of Increased Equity in Federal Contracting." December 1, 2021.

community level is often limited in scale and can lack the flexibility and timeliness to best meet the needs of entrepreneurs and small business owners, the funds can often lead to sparking larger-scale philanthropic and private investment by acting as a first mover.

In St. Louis, for example, Mayor Tishaura Jones launched the Economic Justice Action Plan to drive equitable development by strengthening neighborhoods, closing the wealth gap, improving health and educational outcomes, expanding the tax base, and growing the city's population.[21] This plan was seeded with $246 million in public investment through St. Louis' allocation of American Rescue Plan Act (ARPA) funding to make generational investments in the city with a focus on people and communities that have been historically left out and left behind.[22]



In announcing the plan and commitment of ARPA funding, Mayor Jones said, "Despite these significant resources, this task cannot fall on the shoulders of the city government alone. Turning back decades of disinvestment will require deeper partnerships with financial institutions, non-profit anchors, corporations, foundations, and other organizations to leverage and multiply the investment of public dollars."[23] In working toward the implementation of this plan on behalf of the mayor, the St. Louis Development Corporation brought together the local community foundation, regional and national banks within the city's metro area, and other place-based and corporate philanthropy with an interest in St. Louis. Together, the goal is to leverage the initial public investment to more than $1 billion in total investment by 2030.

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[21] City of St. Louis and St. Louis Development Corporation. "Economic Justice Action Plan."
[22] Lavea Brachman, Joseph Parilla, Glencora Haskins, A.J. Herrmann. Brookings Institution. "From recovery to revitalization: How local leaders are unlocking the potential of the American Rescue Plan." June 12, 2023.
[23] City of St. Louis and St. Louis Development Corporation. "Economic Justice Action Plan."

Role of Place-Based Philanthropy

First, it is important to define place-based philanthropy. Often, place-based foundations are institutions that derive their assets or endowments from sources of local wealth and are created to ensure that there are sustainable sources of capital to meet future community needs. While each community has its own funder ecosystem, several different organizational types can play a role in what we call 'place-based philanthropy.'

This ecosystem may include community foundations; locally-based private philanthropies; health conversion foundations; corporate foundations of businesses headquartered in the area or that have a interest in the community; national foundations that undertake place-based grant-making in local communities or fund national intermediaries that invest locally and regionally; and family foundations or offices of high-net-worth individuals.

An exciting example of a partnership between place-based philanthropy leadership and local government is found in Atlanta's approach to its massive need for affordable housing. In May 2023, the Community Foundation for Greater Atlanta and Atlanta Mayor Andre Dickens announced a $200 million investment in high-quality, affordable housing, prioritizing residents at greatest risk of displacement. The Robert W. Woodruff and Joseph B. Whitehead Foundations committed a collective $100 million to these efforts, intended to be leveraged with an additional $100 million in public funding through a bond initiative.[24]

In announcing this historic new funding, Community Foundation President and CEO Frank Fernandez said, "In every city, the trends have been moving in the wrong direction for entirely too long, and too many people are struggling. But we have a window of time, particularly in the next three years, to change the trajectory in Atlanta. That is why we are moving with urgency to bring together all our partners, to have all hands-on deck, and make a lasting change in housing."[25] While this investment is being applied to the urgent need for affordable housing in Atlanta, it is a compelling example of the type and scale of public-private partnership that could address the urgent small business disparities in communities throughout the U.S.

[24] Community Foundation of Greater Atlanta. "First-of-its-kind Atlanta program leverages $200 million public private investment for affordable housing." May 2, 2023.
[25] Community Foundation of Greater Atlanta. "First-of-its-kind Atlanta program leverages $200 million public private investment for affordable housing." May 2, 2023.

Promising Models for Local Government and Place-Based Philanthropy Partnerships

Place-based philanthropy in partnership with local government, which engages community-focused lenders and business support organizations, can play several different roles in supporting equitable access to capital for diverse small businesses:

1. **Grant funding**
2. **Loan guarantees**
3. **Direct lending, loan participation, and equity or equity-like investments**
4. **Loan purchasing**
5. **Debt remediation**

Here, we take a deeper dive into each category:

1. **Grant funding** for (1) community development financial institutions (CDFIs) and non-profit lenders to build capacity – marketing, outreach, technology, underwriting, servicing – to deliver access to capital and related business support services to more entrepreneurs more efficiently, and (2) underserved entrepreneurs at the formation or growth stages of business to serve as a replacement for or to complement "friends and family" capital that often does not exist or is insufficient to fund low-wealth founders and small business owners.

   CDFIs and non-profit lenders often rely primarily on investments from commercial banks seeking to meet Community Reinvestment Act (CRA) requirements. These commitments can fluctuate depending on a bank's' business activities, and if the need far exceeds current investment levels. For example, when the CDFI Fund released its Economic Recovery Program grant opportunity, nearly 700 CDFIs from across the U.S. requested $7.7 billion in funding, exceeding the amount available by more than four times.[26] Local government and place-based philanthropies can provide additional and more sustainable sources of capital to CDFIs or fund the creation of new CDFIs where there are not sufficient organizations serving the full scope of community needs.

In 2020, an alliance of 17 CDFIs across Pennsylvania (PA) came together as the Pennsylvania CDFI Network to partner with the state to deliver $249 million in small business relief grants ($190 million from PA and $59 million from three nearby communities).[27] A critical component of that successful collaboration was the inclusion of $25 million in grant funding from the PA Department of Community and Economic Development shared across all of the participating CDFIs. This grant funding supported the organizations' operational capacities to deploy the small business relief funds, shored up their balance sheets to allow for future lending, and provided debt relief to small business borrowers in their existing portfolios. This collaborative model was so successful at the state level that it was replicated in Philadelphia, Allegheny (including Pittsburgh), and Lackawanna counties with local support.[28]

Entrepreneurs and would-be entrepreneurs from historically underserved communities (including Black and Latino(a)/Hispanic populations) have been locked out of prior intergenerational wealth creation opportunities and often lack early-stage capital to launch businesses. A 2021 study by the Brookings Institution outlined how the racial disparities in homeownership and home values are "by-products of systemic racism" and identified that Black business formation and growth is limited by lack of homeownership, given the use of home equity as a major source of capital for most people starting new firms.[29] Grants at the formation stage, or other pivotal growth points, made by local government and philanthropic-supported funds directly to entrepreneurs could begin to reverse the massive disparities in business ownership for under-represented founders.

For example, Render Capital's First Dollar Fund provides $5,000 grants to Black and Brown entrepreneurs in Louisville, KY, at the earliest stage of business formation. This program's stated intent and impact is to fill the gap for low-wealth entrepreneurs who – due to systemic discrimination over generations – lack savings and social networks to provide early funding for new business formation.[30]

To create more equitable opportunities for established small business owners to build wealth as they grow, The Foundation for the Carolinas in Charlotte, NC, launched the Beyond Open Fund with a $20 million commitment from Wells Fargo. This initiative provided grants from $5,000 to $250,000 to small businesses specifically to invest in their assets, including equipment, technology, inventory, and real estate.

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[26] CDFI Fund, U.S. Department of Treasury. "CDFI Fund Releases Application Demand for Equitable Recovery Program." February 1, 2023.
[27] PA CDFI Network. "Keeping Doors Open! Investing in Our Most Vulnerable Small Businesses."
[28] PA CDFI Network. COVID-19 Allegheny, Lackawanna, and Philadelphia reports.
[29] Rashawn Ray, Andre M. Perry, David Harshbarger, Samantha Elizondo, Alexandra Gibbons; Brookings Institution. "Homeownership, racial segregation, and policy solutions to racial wealth equity." September 1, 2021.
[30] Render Capital. https://www.render.capital/firstdollar

2. **Loan guarantees** to CDFIs and non-profit lenders to allow them to underwrite differently, including character-based and non-asset-backed lending.

   Banks are the largest source of lending capital for CDFIs.[31] When CDFIs borrow capital from banks to make loans to small businesses in their communities, those CDFIs are obligated to pay back the bank. This repayment obligation for the CDFI remains even if the loans that they make to local borrowers are not repaid fully or on time. While many CDFIs seek grant funding and/or use retained earnings to create loan loss reserves to partially account for this, their reliance on borrowed capital inherently limits the risk they can take.

   This, in turn, impacts CDFI underwriting standards, including how they evaluate creditworthiness and approach the need for collateral and personal guarantees, creating real or perceived barriers for prospective borrowers. Loan guarantees, only drawn upon in the event of an actual default of a loan that a CDFI makes, would allow mission-driven lenders to approach underwriting with even greater flexibility and to experiment with new products designed to better meet entrepreneurs' needs.

   The Council of Development Finance Agencies (CDFA) launched a promising new model of loan guarantees with initial funding from the Robert Wood Johnson Foundation (RWJF). The CDFA's Minority Capital Loan Guarantee Program aims to increase access to capital for businesses in communities that have been historically excluded from opportunity.[32] With funding from RWJF, CDFA has developed a 10-year, $18 million loan guarantee program to help development finance agencies (DFAs) in the United States deliver capital in a more equitable manner. RWJF is providing additional grant funds to support the program's training, continuing education, and technical assistance aspects.

   The CDFA Minority Capital Loan Guarantee Program, which combines a loan guarantee with the adoption of intentional and socially conscious lending practices, targeted marketing, staff training, and community outreach to reduce barriers experienced by socially or economically disadvantaged businesses. Each participating organization can access up to $3 million of guarantee authority and up to a 75% guarantee of small business loans up to $250,000.

   The Tucson Industrial Development Authority has taken advantage of this program to launch the AVANZA Empowerment Fund to provide relationship-based loans with comprehensive pre-application supports and flexible repayment terms to minority-, women-, and veteran-owned small businesses in Tucson, AZ.[33] The CDFA program is substantially over-subscribed in terms of interest from non-profit lenders across the country and could be well-positioned to be replicated in places with local leadership willing to make strategic public and philanthropic investments.

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[31] AERIS. "CDFI Loan Fund Capitalization: The Continued Importance of Bank-CDFI Partnerships." January 2023.
[32] Council of Development Finance Agencies. https://www.cdfa.net/p/mclgp.html
[33] Tucson Industrial Development Authority. https://www.avanza.fund/

3. **Direct lending** to underserved small businesses and entrepreneurs, **loan participation** with CDFIs and non-profit lenders, and **equity- or equity-like** investments.

Direct lending by local government or philanthropy-backed funds adds to the options available to entrepreneurs, especially if done in a coordinated fashion with local CDFIs and other non-profit lenders. Loan participation would allow CDFIs and non-profit lenders to share risk across their loan portfolios and increase the overall pool of capital available to entrepreneurs without taking on additional on-balance-sheet debt. Philanthropic and public investors have different return profiles to allow for more flexible forms of equity- and equity-like capital.

In addition to the strong city-philanthropy partnership in Atlanta around affordable housing highlighted earlier, the GoATL Community Capacity Fund, operated by the Community Foundation of Greater Atlanta, was seeded in 2018 with a $10 million investment from the foundation's unrestricted capital and has since raised close to $5 million in additional investment from donor-advised funds. This pilot fund explicitly sought to build CDFI capacity in Georgia by addressing gaps in the market across diverse thematic areas, from access to affordable housing and quality education to preserving organic farmland and contributing to small business development.

In 2022, the Community Foundation for Greater Atlanta expanded its efforts by adding two additional funds: 1) the GoATL Economic Inclusion Fund and 2) the GoATL Affordable Housing Fund.[34] The GoATL Economic Inclusion Fund, in particular, has an explicit mission to drive equitable job growth and wealth creation by investing directly in historically marginalized, BIPOC- and women-owned small businesses. This 10-year fund made its first investment in 2023, has raised more than $5 million to date toward a target of $25 million, and aims to achieve a 4% IRR for investors. It lends up to $1.5 million for up to a 7-year term directly to growth-stage businesses and participates in loans with CDFIs to ensure that the foundation is not competing with mission-oriented lenders in the marketplace, but rather complements their offerings and fills gaps.

Crunchbase found that Black entrepreneurs only received 1.2% of venture funding in 2022.[35] Equity funding from friends and networks is likely also significantly lower for Black entrepreneurs based on the extreme wealth disparities between entrepreneurs of color and White entrepreneurs. Local government and philanthropy leaders can help communities start new funds, derisk funds through philanthropic dollars, help start crowdfunding platforms, and more in this space.

The Innovative Finance Playbook, released in December 2022 through a collaboration among Catalyze, the Nowak Metro Finance Lab at Drexel University, and the U.S. Economic Development Administration, showcased promising models to address these gaps. For example, the Greater Colorado Venture Fund combined public investment from the state and federal governments with private philanthropy,

[34] Community Foundation of Greater Atlanta. https://cfgreateratlanta.org/togetheratl/goatl-fund/
[35] Chris Metinko; Crunchbase. "Special Series: VC Dollars to Black Startup Founders Fell More Than 50% in 2022." February 22, 2023.

including the Gates Family Foundation, to create a $17.5 million venture fund. This fund invests in seed-stage businesses located in rural Colorado, which are often overlooked by traditional venture capital providers.[36]

Collab Capital was founded in 2019 and makes early-stage investments in Black-owned companies in the top 25 U.S. cities with a high concentration of Black entrepreneurs and a low concentration of risk capital. Collab explicitly focuses on a mission to create, grow, and sustain wealth in the Black community, which it executes with a profit-share approach to funding that is paired with industry expertise and social capital. The Andrew W. Mellon Foundation is one of the investors in Collab's first $50 million raise, alongside a wide range of corporate investors.[37]

4. **Loan purchasing** from CDFIs and non-profit lenders to increase their liquidity and ability to do more direct lending without taking on additional debt to their balance sheets.

   Similar to commercial financial institutions that raise capital for new lending by selling all or portions of their existing loan portfolios, CDFIs have the opportunity to package and sell their loan assets to willing buyers. This frees up their balance sheets to make loans to new borrowers. Engaging local government and place-based philanthropy in this market would create a broader pool of purchasers for CDFIs to engage, grow the secondary market for small business loans, and allow CDFIs to serve more borrowers without themselves taking on more debt.

   A national organization, Community Reinvestment Fund, USA (CRF), has been active in this market for decades. CRF serves as an intermediary by buying assets and securitizing them to drive liquidity in the market for CDFIs and non-profit lenders, and it currently manages $2 billion in assets through its S&P-rated back office servicing platform.

   In June 2023, CRF, Calvert Impact, and the National Development Council released a report that outlined how recent place-based relief efforts to address the devastating impact of the COVID-19 pandemic on entrepreneurs show the way toward building a sustainable secondary market for small business loans. Public and philanthropic investors together provided $500 million to support a series of funds across multiple states that provided capital to more than 5,500 small businesses through almost 40 different mission-driven lenders. Nearly 70% of the businesses were led by people of color and/or women, most of whom had never borrowed money for their businesses before.[38]

   The public investors in these funds spanned all levels of local government, including cities, counties, and states. In this model, special purpose vehicles were created to purchase 95% of the loans made by the

[36] Catalyze, the Nowak Metro Finance Lab at Drexel University and the U.S. Economic Development Administration. "Innovative Finance Playbook: Greater Colorado Venture Fund Case Study." December 2022.
[37] Catalyze, the Nowak Metro Finance Lab at Drexel University and the U.S. Economic Development Administration."Innovative Finance Playbook: Collab Capital Case Study." December 2022.
[38] Calvert Impact, CRF USA, and NDC. "Small Business Community Finance: Scaling with Integrity." June 2023.

CDFI lenders, providing that capital back to the CDFIs to lend to additional borrowers. The report highlighted that for every dollar received by CDFIs, they could make $20 worth of small business loans.

Cities from Los Angeles to New York are exploring the development of public banks. While there is a wide range of forms that this could take in different places, each with its own challenges and complexities, local government participation in loan purchasing from local CDFIs could be an alternative way to meet the intent or could be included as a key component of the role that a public bank would play. As with any other financing tool, the source of public capital would need to match with the risk and return profile.

5. **Debt remediation** for individual entrepreneurs.

Diverse entrepreneurs are often saddled with a higher debt load. Researchers at the Federal Reserve Bank of St. Louis found in 2022 that not only are there disparities by race and gender in holding student loan debt, but those disparities also grow over time.[39] Student loan debt relative to educational outcomes is higher in diverse communities. Also, lower credit scores create challenges in obtaining both traditional and non-traditional credit. Local government and philanthropy can develop debt remediation strategies like loan forgiveness funds and credit repair support that improve the likelihood of obtaining business credit.

A 2020 Ewing Marion Kauffman Foundation brief explored the relationship between student loan debt and entrepreneurship.[40] Their research noted that there are various and intersecting relationships between taking on student loan debt to pursue higher education and the path to entrepreneurship. One key finding was that higher levels of student loan debt among entrepreneurs are negatively correlated with the income of their businesses and the number of employees. Further, student loan borrowers reported that their debt was a factor in their decision or ability to start new businesses.

This reinforces the earlier findings by researchers at the Federal Reserve Bank of Philadelphia, who analyzed the effects of student loan debt on net small business formation. Their 2015 analysis found that a certain level of increase in student debt had the impact of reducing the number of small businesses with one to four employees by 14%. The researchers concluded, "Given the importance of an entrepreneur's personal debt capacity in financing a startup business, student loan debt, which is difficult to discharge via bankruptcy, can have lasting effects and may have an impact on the ability of future small business owners to raise capital."[41]

[39] Ana Hernández Kent and Fenaba R. Addo; Federal Reserve Bank of St. Louis. "Gender and Racial Disparities in Student Loan Debt." November 10, 2022.
[40] Ewing Marion Kauffman Foundation (2020), Student Loans and Entrepreneurship: An Overview, *Entrepreneurship Issue Brief*, No. 5, Kansas City, Missouri.
[41] Brent W. Ambrose, Larry Cordell, and Shuwei Ma; Federal Reserve Bank of Philadelphia. "The Impact of Student Loan Debt on Small Business Formation." July 2015.

In light of the recent shifts in federal policy around student loan forgiveness, it would be timely for local leaders to jointly explore policies or investments that could retain more diverse talent in cities and foster stronger pathways to entrepreneurship through initiatives to ease the burden of student loan debt.

Local Government & Philanthropy Can Lead Together

Each of these models is customizable, replicable, and scalable to align with local communities' through a combination of strong leadership, public funding, and place-based philanthropic capital. Mayors can play a unique leadership role in laying out a compelling vision, aligning local stakeholders, and seeding innovation with public resources to support equitable access to capital for business formation and growth. The mayor and other government officials can establish and communicate a bold vision, set goals for investing in historically disadvantaged entrepreneurs, develop and support innovative strategies, convene ecosystem players, provide seed capital, leverage existing and new public funding, and help attract private funding. Place-based philanthropic and corporate funders must be ready to invest alongside the public sector, and economic development organizations, CDFI lenders, and venture capital partners will be the vehicles to develop and deliver capital.[42] We hope that this piece provides an actionable roadmap of replicable models and opportunities for government leaders and funders at all stages.

As we conclude, it is important to note that increasing access to funding is only part of the solution. Inequitable access to credit and capital has created inequity in small business startups and business growth in the United States. However, providing more capital without considering other barriers experienced by Black, Hispanic, Asian, Native American, and/or Multi-Racial small business owners will only partially improve their condition. The ability to start and grow businesses occurs within a broader environmental context: the entrepreneurship ecosystem.

The entrepreneurship ecosystem includes coaching and training on starting and growing a business, accessing the necessary professional services and capital providers, and developing relationship networks to identify

[42] Adapted from *Vision Philadelphia: Access to Capital for Philadelphia's Diverse Business Owners* co-authored by M. Yasmina McCarty, Anne Bovaird Nevins, and Kevin S. Dick.

market opportunities and form partnerships. Also, entrepreneurs start and grow in communities with specific cultures and government policies that can support or detract from equitable outcomes. In this piece, we have laid out capital access strategies for local government and place-based philanthropy that will require a strong network of CDFIs or other mission-based lenders, alongside a robust set of business support services providers and other critical actors to be implemented. If those organizations do not exist or have insufficient capacity on the ground locally, those gaps will need to be addressed first. By supporting the development of an equitable entrepreneurial ecosystem in their community, local government and place-based philanthropy can jointly influence more equitable small business outcomes.

Please stay tuned for part two of this series, which will dive further into the role that local government and place-based philanthropy can play in supporting equitable entrepreneurial ecosystems.