Appalachian Capital Policy Initiative
Project Summary

July 2012

Introduction

The Appalachian Regional Commission (ARC) has determined that access to capital and credit is one of the major factors limiting business creation, expansion, and growth in the Appalachian region. This has been a historic problem in the region relative to many other parts of the country. Previous ARC studies in 1998 by Mt Auburn Associates and in 2007 by the National Community Reinvestment Coalition found that:

- That there was a significant gap in the availability of equity capital relative to other areas of the country. For example, just 1.3% of professionally managed venture capital is invested in Appalachia annually.[1]

- Established small businesses in the region -- and particularly small firms with fewer than 10 employees -- had insufficient financing to expand. For example, lenders using the SBA 7a program made 15% fewer loans in Appalachian as compared to the nation, while 7a loans in ARC designated Distressed Counties were just 1/3 the national average.[2]

- Non-metropolitan and distressed counties had considerably smaller shares of bank assets, which resulted in these communities receiving less community development financing.

Other data reveal that of the $26 billion in New Markets Tax Credit allocations provided across the nation, only 11 funds are located in Appalachia (4.4% of funds) and have received just $290 million in tax credit allocations (1.1% of allocations). Similarly, of the nearly 3,000 projects that have received $15.8 billion in financing from New Markets funds, just $600 million has been invested in Appalachia - or 3.8% of total New Markets investment dollars. Appalachia made up about 8% of the U.S. population in 2009, while 45% of Appalachia by geography is eligible to participate in the New Markets program.[3]

These challenges have only been intensified by the severe recession and by longer-term trends that have been increasingly driving economic activity and population into larger metropolitan areas. According to a recent report by the Brookings Institution, the top 100 metro areas are now home to approximately two-thirds of all Americans.

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[1] National Venture Capital Association, PricewaterhouseCoopers/Money Tree Report, 2010.
[2] US Small Business Administration, 2003.
[3] US Department of Treasury, CDFI Fund, CIIS data, September 2010.

In addition, Appalachia and other rural regions have also been hurt by the ongoing consolidation and related changes taking place in the banking industry. Larger banks have been consolidating in major cities and urban regions, and there are fewer community banks, particularly in smaller towns and rural areas. These trends have been building for many years but have been accelerated by the current economic downturn. This is particularly noteworthy as the presence of banks, bank branches, and bank capital positively correlates with increased business lending in rural Appalachian communities (2007, National Community Reinvestment Coalition study).

Over the past several decades, a number of programs and initiatives have been mounted to deal with the issues of capital and credit availability and access to debt and equity capital in Appalachia, often with ARC support. A network of Community Development Financial Institutions (CDFIs) has been created at leading regional non-profits in most Appalachian states, and there are 35 publicly supported Revolving Loan Funds (RLFs) operating in the Region as well. ARC has supported the formation and expansion of microenterprise loan funds. And it has directed funding to seven active development venture capital funds in the region, as well as helped create New Markets Tax Credit CDEs.

These efforts provide a foundation to build upon as ARC and its local and state partners consider what additional actions are needed to deal with current and future economic challenges.

Objectives

The Appalachian Capital Policy Initiative has four objectives:

1. To expand bank lending for business expansion and growth;
2. To attract new sources of equity investment into the region from private corporations, pension funds, national financial institutions, philanthropic institutions, and intermediaries;
3. To build the capacity of local/state CDFIs, loan funds and other providers of capital, and to help existing CDFIs expand (where needed) into underserved communities;
4. To increase the volume and quality of deal flow and financeable transactions.

Strategy

To accomplish this, ARC proposes to develop a multi-faceted strategy that can: influence public policy; educate key constituencies and enlist their support and participation; develop and expand programs that deliver capital to business; and attract new sources of capital to the region.

This initiative will be aimed at developing an overall policy framework for addressing capital and credit availability over the long-term, and identifying and implementing specific actions that can improve and expand capital access in the near-term.

Staffing and Timeline

This initiative is a key element in the current ARC Work Program. Ray Christman, former head of the Federal Home Loan Banks of Atlanta and Pittsburgh, is serving as advisor to the ARC Federal Co-Chair on this project and is providing strategic guidance and oversight. He is supported by ARC staff and other resources as required.

An action plan has been developed with the help and input of a Capital Policy Advisory Committee, comprised of representatives from financial institutions, CDFIs, state governments, venture funds, and other key points in the region (see attached). This Advisory Group provides oversight and direction for the assessment of strategic options to address the Region's capital and credit challenges. To date, Advisory Committee meetings have been held in December 2010, February 2011, October 2011, and March 2012.

This initiative is expected to continue through 2012 with key work program items being acted upon and implemented at different stages.

Work Program

The current work program for this effort, developed with the help of the Advisory Committee, includes four major areas of emphasis:

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I. Attracting New Capital to Appalachian CDFIs
   a. Capital raising for CDFIs. Implement a strategy to attract new capital from traditional (philanthropy, federal programs, financial institutions, etc) and non-traditional (Fortune 50 companies, utilities, etc) sources. A business plan has been developed for the formation of a financial intermediary to bring new capital to existing CDFIs, CDCs, RLFs, and other development lenders, including utilization of the new CDFI Bond Guarantee Program. Conversations with funders are on-going.
   b. Partnership with US Department of Treasury - CDFI Fund. ARC is working with the CDFI Fund as part of the federal interagency Appalachian Regional Development Initiative MOU to target products and services to underserved geographies, including ARC states with limited CDFI activity and /or use of programs such as New Markets. Activities include the development of new CDFIs in Ohio and Alabama, and the formation of New Markets Tax Credit CDEs in West Virginia and Mississippi.

II. Build Entrepreneurial Ecosystems

a. A 'Startup Appalachia' Initiative was launched by the Appalachian Funders Network, modeled after the national Startup America program. ARC is working with the Appalachian Funders Network, USDA Rural Development and other partners to craft an action plan to implement this initiative in the Region. Focal points include the targeting of three promising sectors - energy and entrepreneurship; food systems; and health care and entrepreneurship.
b. An Angel Investment Fund initiative was launched in April 2012. ARC is working with RAIN Source Capital to bring successful existing angel fund strategies to the Region. Targeted Angel Funds are initially being developed in several states including: Ohio, West Virginia, and Virginia.
c. Formation of a regional SBA Impact Investment (Venture Capital) Fund for Appalachia is being developed by partners in Northern Appalachia.

III. Expand Bank Lending in the Region

a. Expand use of SBA 7a in the Region. In partnership with State Banking Trade Associations, work to promote the use of packaging and servicing organizations among community banks.
b. A series of educational workshop has been held with the Federal Reserve, the Office of Comptroller of the Currency, and FDIC aimed at helping community banks understand the availability federal resources and programs to help finance their business customers. State banking trade associations and state banking supervisors have helped co-sponsor and encourage banks to attend these sessions. To date, sessions have been held in WV, TN, and KY.
c. FDIC Alliance for Economic Inclusion program. FDIC and the West Virginia Development Office are working to implement the AEI program in WV. This program helps expand bank resources to underserved areas, and engages non-profit and public sector partners to participate in related activities.
d. Develop and hold export finance workshops. ARC is working with leading International Trade Centers to craft suitable training programs.
e. Advocate for modifications to CRA that would make investments and loans in rural areas like Appalachia more attractive to financial institutions.

IV. Research / ARC activities

a. A research study is underway to update data on capital and credit gaps, bank presence and lending activity, and related issues in Appalachia. ARC has contracted with the National Community Reinvestment Coalition to complete this study.
b. Revise ARC RLF guidelines, in partnership with Development District Association of Appalachia. This activity is under development by ARC staff.

For further information on the Capital Policy Initiative, please contact:

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