Community Investment Trust Summary

Investcit.com

Lower income Americans across the country face similar barriers to building personal wealth, which include insufficient experience with money management, and a lack of financial products suited to their means and desires. The resulting lack of financial resilience leaves them vulnerable to even a small financial calamity, often at a high cost to the people themselves and the resources of social safety net programs. We believe that the CIT can be a powerful tool in empowering people to have a direct hand in improving their own financial health as well as their community's health and prosperity.

Mercy Corps took a deeper insight into asset poverty and financial inclusion, and constructed an investment product using existing financial mechanisms but re-aimed them for low-income people. We learned from conversations with community leaders at churches, schools and with elected officials. We held focus groups with people in affordable housing buildings. We discovered that people were motivated but had little income to invest, were not budgeting effectively and did not understand investments. They had debt but no assets. These issues are addressed through our financial action curriculum, which we created to educate community members as a precursor to investing (see page 8). We call our project and investment product the Community Investment Trust (CIT). The CIT addresses the intractable household financial challenges of asset poverty, personal financial inaction and the inaccessibility of financial products, and the long-standing community economic development challenges of financial inclusion, equitable development and inclusive growth.

Our model is informed by the intersection of marketing, economics and psychology, a connection known as behavioral economics, an approach to tap people's behavioral action to improve their lives. The CIT is a community economic development tool, and is unique to the investment market because 1) it includes lower income people in real estate development; 2) fits a low-income investor's budget with monthly low-dollar investments of $10, $25, $50 or $100; 3) includes financial planning and action education and 4) has downside risk protection for investors through a direct pay letter of credit. The nature of the low-dollar monthly investment creates an ownership path for hundreds of investors in any project with a capitalization of over $1 million. Plaza 122 in Portland, Oregon is a first example of this, with a potential for 300-500 investors in four zip codes.

Plaza 122 in Portland, Oregon

The two buildings of the 29,000 sq. ft. Plaza 122 hold 27 business and non-profit tenants that reflect the vitality and diversity of the neighborhood. They include a Latina-owned hair salon, Somali-owned taxi company, Russian-owned lotion business, health and wellness entrepreneurs, a low-cost funeral planner, accounting and tax preparation firms and non-profits including faith-based organizations, the Somali Association of Oregon, Pathfinders of Oregon and TransActive Gender Center.

How to Move from Owing to Owning

Our research and surveys indicated that people uniformly wanted access to information on investing and expressed specific interest in being part of something larger, like a commercial real estate property in their neighborhood. Local ownership assures investors a visceral and mutually reinforcing connection to the commercial property with business and non-profit tenants that investors know and will patronize in their own neighborhood.

The ownership model we chose is the REIT (Real Estate Investment Trust), which was created in 1960 to facilitate the aggregation of ownership in real estate by a minimum of 100 investors. We will decide on the REIT tax election after we have 150 investors. Up until our project was formulated, private REITs were the domain of only wealthy "accredited" investors. We want to turn the REIT on its head and offer it to unaccredited investors, opening up an asset building path for all at a monthly investment level that is low enough to assure access for all ($10-$100/mo.), which will widely distribute the ownership opportunity in a neighborhood. A key and unique element to the CIT is that we have loss protection for investors through a bank issued letter of credit.

Project Description and Location

MCNW chose the Mill Park / Hazelwood neighborhood and its surrounding four zip codes in SE Portland, an area of ethnic diversity and strong community groups, schools and churches. Census information indicates that the neighborhood is populated by families matching our targeted investor.

- Median family income is 67% of the Portland metro area median income
- The poverty rate is 22%
- Only 35% of homes are owner-occupied
- 90% of students at nearby Mill Park Elementary qualify for the free/reduced lunch program
- Significant ethnic diversity with refugees, immigrants and people displaced by gentrification

CIT Outcomes and Impact

We seek impact on the household level, the neighborhood level and for the commercial property and its business tenants. Investors in the first CIT will come from four zip codes (97216, 97230, 97233 and 97236) an area surrounding Plaza 122 with approximately 185,000 residents. The CIT addresses financial inclusion and creates access for people to financial products and personal action.

The CIT will produce both short-term and long-term impact on three levels:

1) Individuals/families (the CIT Investors)
2) CIT commercial property performance and tenant success
3) Neighborhood and its organizations (schools, churches, housing agencies, neighborhood groups)

The CIT provides the following positive community development impacts:

1) Affordable multiple-use business space
2) Diverse tenant mix meeting neighborhood needs
3) Ressurection of a foreclosed property

The CIT will help build a culture of fiscal literacy and financial success

The CIT enables small, incremental direct investments into community-owned commercial property. Aggregating small-dollar investors broadens the base of people who are working toward the same goal in their neighborhood. With an emphasis on neighborhood stability and vitality, the CIT embodies Mercy Corps creative and collaborative approach to developing propserity and resiliency within communities. By tapping into the universal desire of people to succeed and to control their own destiny, and providing the tools for them to realize those desires, the CIT model empowers a community and its neighborhoods to build a more prosperous future. **We believe that what is working in Portland is transferable and scalable for communities across the country.**

CIT Replication Steps and Goals:

1. **Identify Partners** and/or a foundation partner to support the replication of the CIT model in places of need and with a lead organization in each location with the capacity to create and manage a CIT. Build our internal capacity and refine the CIT Toolkit to fit other regions and property types to the build the capacity of other Nonprofits / Cities / Churches / Economic Development Agencies to effectively replicate the CIT Model.

2. **Maintain Focus on Improving Financial Decision Making** – Through engaged community leadership, fiscal literacy trainings, and shared learning, community members will improve financial planning and decision making.

3. **Increase Finanical Inclusion, Equitable Development and Reduce Asset Poverty** – Among low-income communities and with renters in diverse urban and rural communities by providing investors a path to build assets by investing in profitable CITs.

4. **Improve Community Health** by engaging community members in a common cause to increase community safety, unity, and community engagement through making an investment in the community in which they live.

The CIT Tool Kit will be licensed to authenticate CIT replication anywhere in the US. The Tool Kit to create a CIT includes:

Products for Initial Replication License

1. Organizational Self-assessment Tool
2. Community Mapping Tool
3. Property Evaluation Tool
4. Property Financial Spreadsheets
5. Capitalization Options: Debt / Subordinated Debt / Equity / Grant Subsidy
6. Investor Training and Curriculum
7. Legal Framework and Entity Formation
8. Communications, Public Relations Guidance

Products for Annual Service Fee

9. Website: InvestCIT.com
10. Access to Online Investment Management Portal and Customer Service Provider
11. REIT Management, Investor Management and Investor Protection Back-stop
12. Annual Monitoring, Evaluation, Research, Learning and Impact Evaluation
13. Community of Practice Sharing with Licensees

Building an on-ramp to a culture of fiscal literacy and financial action

How Mercy Corps' Community Investment Trust is helping lower income individuals make their first financial investment in real estate

Policy paper

How can we help people with lower incomes save and invest?

One in three Americans are not saving any money, and one in four Oregonians, like most of the nation, live in a condition of 'asset poverty' (Sparshott 2014; CFED 2015). After three months without income, individuals living in 'asset poverty' are unable to meet basic needs without assistance. Traditional advice to lower-income individuals has been to pay off credit card debt and build an emergency fund before they even consider investments, and then to consider diversified investments like mutual funds. While this is good advice in a general sense, it does not translate well into a program that changes financial behavior. A range of practical and psychological obstacles tend to work against making these significant changes in financial behavior. What is needed is an 'on-ramp' which helps people who have not invested to make small, concrete changes in a supportive environment to engage in positive long-term financial decisions for the first time.

This paper presents a case for looking at investment opportunities for people with lower incomes not just from the perspective of whether the opportunities are the theoretical optimum investment, but also whether they support the goal of helping to make decisions for good long-term financial health more likely. This paper focuses on the individual behavioral, economic, and social aspects of Mercy Corps' Community Investment Trust (CIT)[1] program, and does not address the community benefits of the program, except to the extent that they influence individual decision-making.

When we're designing financial literacy (or financial action) training we must understand that in the real world simply delivering knowledge does little good. Mercy Corps' CIT is an investment option that accompanies a financial education program. These two elements have been designed to give high quality financial literacy training and, for those who are a good fit, access to an investment opportunity that generates an annual dividend and good long-term returns at no or low risk. Beyond those basics, every element of the program has been designed to take advantage of research about how we can make it easier for people in poverty to make good financial decisions.

[1] CIT is our term for what may become a private REIT (Real Estate Investment Trust), which was created in 1960 to facilitate the aggregation of ownership in real estate by a minimum of 100 investors. Up until our project was formulated, private REITs were the domain of only wealthy "accredited" investors.

Good advice is not enough to change behavior – what economic, behavioral, and cognitive research tells us about behavior change

There has been significant interest in recent years in 'behavioral economics,' the study of the effects of psychological, social, cognitive, and emotional factors on economic decisions. This research highlights the differences between what the 'rational economic actors' of neoclassical economics might be predicted to do, and what people actually do in the real world. Neoclassical economics assumes that 'rational economic actors' have the information they need; can process this information correctly and completely; and have preferences that are not affected by anything other than payoffs of their decisions. Their preferences are assumed to be predetermined and stable across time. The considerable resilience of neoclassical models of human behavior have led to approaches on giving people more information or providing people incentives and tools to help them make better decisions in their financial life.

The assumption used to be that rational actors with better information would make better choices, but the reality is that a range of other factors have much more impact on behavior than raw financial information. These other factors include, but are not limited to, how choices are framed; preferring the present to the future; overestimating how well off finances will be in the future; valuing losses more than gains; having short attention spans or tendencies to forget; adhering to social norms; and preferring default options. These issues apply across all financial groups, but because poorer people have fewer resources, and less of a margin of error, there is a greater imperative to deploy them in the most efficient manner.

Human behavior is governed by two separate systems. One system involves making quick decisions in familiar circumstances, and the other system involves making deliberate decisions in complicated or unfamiliar circumstances (Kahneman 2011). Unfortunately, reconciling these two systems is not easy (Heath and Heath 2010; Kahneman 2011). That said, we now know quite a lot about how to make it easier to keep the two sides of our motivation in balance, and make good long-term financial decisions while also attending to our needs and quality of life in the present.

Here are five examples of the factors that research has highlighted in the last few years that influenced the design of Mercy Corps' Community Investment Trust. They highlight how design of interventions and financial offerings can strongly influence participants' decisions both in the short and long term:

1. Too many choices leads to inaction

Dean Karlan's[2] research found that many factors unrelated to the economics of a decision weighed heavily in people's decision making. For example, giving consumers only one choice of loan size, rather than four, increased up-take just as much as reducing the interest rate by 20% (Bertrand et al. 2010). Rich and poor people alike can be overwhelmed by choice - Columbia Business School psychologist Sheena Iyengar found that supermarket shoppers presented with a wider selection of jams bought less jam than those presented with a smaller selection (Iyengar and Lepper 2000).

While the CIT's financial planning and action education offers many different options in the curriculum (depending on factors such as risk tolerance level, amount of money available etc.), for those

[2] Professor of economics at Yale, President of Innovations for Poverty Action, research affiliate MIT Poverty Action Lab.

investors who are interested in real-estate investing, there is only one option offered - the CIT. The curriculum, paired with an immediately available investment option in the CIT, connects learning with action in a structured way. Research shows that any benefits that (may) arise from more than one choice are more than cancelled out by the reduced uptake of programs with more than one option (Iyengar and Lepper 2000; Iyengar, Huberman and Jiang 2004; Botti and Iyengar 2006; Schwartz 2009).

2. Vivid, concrete, and tangible investments are compelling

The fact that people are more strongly impacted by a potential loss than they are compelled by a gain of the same magnitude is called 'loss aversion'.[3] In the banking field, loss aversion translates (somewhat counter-intuitively) into a psychological sense that spending now is 'in hand', whereas putting money into a savings or investment for the future is psychologically a 'loss'. Research suggests that people are more inclined to use savings accounts if they are named for their intended use (for example 'retirement', 'education' etc.) (Thaler 1999). Making investment choices 'vivid, concrete, and tangible' maximizes people's willingness to use them (Karlan 2010). Local real-estate investment scores highly in each of these areas, making it a compelling investment psychologically, and offering a convenient, immediate, and accessible opportunity for financial action.

3. Inertia tends to work against change

Perhaps depressingly, the best predictor of future behavior is current behavior. To overcome this tendency to revert to our habits, behavior change needs to be made easy. Even seemingly small roadblocks between a message, and the opportunity to act on it, can be significant. For example, in one experiment one group of poor farmers was offered the opportunity to place earnings in a savings account that they could open on the spot, while others were told about the account, but were not able to open it for several days. A control group was not told about the account. Fifty seven percent of farmers who immediately paid into the account bought fertilizer for the next year, compared to only 17% in the control group (Duflo, Kremer and Robinson 2006 quoted in Bauer 2014). Interestingly only 30% of the group who were told, but had to wait to open the account bought fertilizer (Duflo, Kremer and Robinson 2006 quoted in Bauer 2014). They typically reported that they wanted to, but when the opportunity came to open the account several days later they did not act. People find it hard to overcome inertia – an immediate opportunity to act, rather than an abstract intention to do it in the future helps – a lot – that's why Mercy Corps offers training to participants for whom the investment is a good fit and the opportunity to enroll is immediate.

4. It is hard to pay attention and stick to decisions

Keeping financial decisions high on the 'to-do list' is hard, especially when there are many competing priorities. Mercy Corps is using a variety of methods to help people stick to decisions. Perhaps for this reason, higher income people typically automate savings and retirement plans, helping them stick to goals by removing the need to regularly act. Absent these elements, structural changes to reducing obstacles and other supports can help encourage people to stick to their commitments (Hall, Galvez and Sederbaum 2014). Making sure that investments remain salient by using community networks and groups to help people remain accountable to their goals (Karlan et al. 2009). Recruiting churches, housing associations, and other social groups to help keep the issue on the agenda is one way to make sure that it remains a top priority. In addition to larger group support, each participant will be paired with an individual mentor who can help them stay

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[3] The pioneering work on this was done by Kahneman, Knetsch, and Thaler, but it has been replicated in many studies. Kahneman was awarded a Nobel Prize for his work on this and related ideas in 2002.

accountable to the plan they made. Making investment behavior regular and predictable is another factor that contributes to success – once a participant makes a budget plan and identifies their saving or investment margin they will be coached on making themselves personalized reminders.

5. What we think other people are doing is hugely influential

Social pressure is a powerful influencer of behavior. From the pioneering work on peer and authority pressure in the social psychology of the 1950s to current social media advertising, the power of peers and role models to influence behavior is enormous (Thaler and Sunstein 2008). In an experiment in Minnesota in 1996 groups of taxpayers were given four different kinds of information. Either a) that their taxes went to pay for various beneficial things, b) information about risks of punishment for non-payment of taxes, c) information on how to get help filling out their tax forms if they needed it, or d) that 90% of Minnesotans paid their taxes fully. Only the fourth item (that reinforced social norms about tax payment) had a positive effect on reported income taxes paid (Coleman 1996). Related research has indicated that stigma and stereotyped beliefs about those living in poverty can also consume mental resources and impair cognitive performance (Hall, Zhao and Shafir 2014). The Community Investment Trust seeks to improve trust through mobilizing the power of taking individual action while being part of a group of people who are challenging social stereotypes, building self-esteem and community connections.

Research-driven design for transformational change – an 'on-ramp' to better financial decision making

Mercy Corps believes we should not be designing financial education and other interventions solely around optimized financial instruments. Rather we need to design for the real social, economic and behavioral situations that people find themselves in. Mercy Corps' CIT program takes current best practices in behavior change and applies them to the real problems facing people on low incomes.

Criticisms of offering community-based real-estate investment to lower income people focuses on ways in which other choices might show higher effective returns on paper. Typically, critics will suggest that paying down debt, building emergency funds, and diversified financial instruments are top priorities. While this advice is not bad in theory, it fails to take into account the behavioral economic factors that result in it rarely being followed in real life. When the science of behavior is applied to changing financial practices, an 'on-ramp' to better financial decision making and literacy can be built that will help individuals and communities transform their financial futures.

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Moving from Owing to Owning Curriculum Overview

Session 1: Creating an Owner Mindset

- *What participants will learn:*
    - How to lower what you owe and increase what you own
- *What participants will do:*
    - Figure out your current wealth and compare with financial goals
    - Create a budget for savings and long term investment

Session 2: Getting in Line with your Goals

- *What participants will learn:*
    - Address the gap between financial goals and current net worth
    - Improve credit score
- *What participants will do:*
    - Take action on the gap between personal wealth and goals
    - Take action on credit report and improve credit

Session 3: Investment Options for matching your Goals

- *What participants will learn:*
    - How various investments work and their risks/benefits
- *What participants will do:*
    - Identify potential barriers for saving and investing
    - Create a plan to stay on track with financial goals

Session 4: Creating your Investment Plan

- *What participants will learn:*
    - How to select and purchase investments that fit financial goals
- *What participants will do:*
    - Evaluate the suitability of certain investment options
    - Create an investment plan to help achieve financial goals