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# **Emerging Domestic Market Advisory Group Progress Report #1**

The Assembly Jobs, Economic Development, and the Economy Committee (JEDE) is the policy committee within the California State Assembly responsible for examining issues related to capital formation, among other economic development policies, programs, and services.

## **Section I – Introduction**

In October of 2007, the Assembly Committee on Jobs, Economic Development, and the Economy (JEDE) convened an advisory group of investors and other economic professionals to examine how to attract private sector investment to California's lower income communities.

This report lays out a summary of the Advisory Group's first four months of activities, including objectives, projects, and recommendations for future actions. A list of the members of the Advisory Group has been included in the Appendix of the report.

Additional information on meetings and analytical work of the Advisory Group is available on the JEDE website at:

<http://www.assembly.ca.gov/acs/newcomframeset.asp?committee=131>

The JEDE Committee formally thanks its partners and collaborators on this project, the California Latino Legislative Caucus and the California Hispanic Chambers of Commerce.

### Emerging Domestic Markets in California

Driven by significant demographic changes and their related impacts on markets, institutional investors had begun to target small portions of their portfolios to underserved communities and businesses that historically lacked access to capital, also known as emerging domestic markets.

The term "emerging domestic markets" refers to people, places, or businesses with growth potential, which have historically faced systemic capital constraints. The demographics of emerging domestic markets include ethnic- and women-owned firms, urban and rural communities, companies which serve low- to moderate-income populations, and other small- and medium-sized businesses.

To better understand the dynamics of the new and growing investment area, the JEDE Committee decided to directly engage the investment community in an extended

conversation about what impediments they encounter in trying to invest in emerging domestic markets.

While not every-low income community in California is ready for private sector investment, many communities and small businesses could become investment ready through more effective partnerships between the nonprofit, private, and public sectors.

Although institutional investor activity in emerging domestic markets is small by their standards, these "small" investments represent significant new economic and community development funding for California communities.

Already, both California Public Employees Retirement System (CalPERS) and the California State Teachers Retirement System (CalSTRS) have adopted an EDM investment goal of 2% of their entire portfolio. CalSTRS' exposure in California's underserved and emerging markets was \$2.3 billion as of December 31, 2006, representing a \$364 million increase from the previous year. California has no other similar program that can outpace the volume of investments large institutional investors could make in our lower income communities and minority- and women-owned businesses.

## **Section II – Primary Object and Projects of the Advisory Group**

This section provides information on the primary objective and projects of the Advisory Group.

### Primary Objective

The Advisory Group set a long-term objective to have investments in emerging domestic markets be considered as a sub-asset class for investments by institutional investors. In reaching this objective, the Advisory Group chose three issues to address:

1. Enhance the financial literacy of entrepreneurs seeking debt and equity capital;
2. Develop one or more models for deploying private equity funding in early-stage companies, including blending public and private resources to meet risk-adjusted return requirements; and,
3. Establish common definitions and criteria for use by investors in emerging domestic markets.

### Projects of the Advisory Group

The Advisory Group worked on several projects, each designed to improve the ability of private investors to take actions in emerging domestic markets, including providing the framework for a web-based directory of capital, supporting the update of a community

development dictionary, and hosting one or more regional investment roundtables. Each of these projects is described in greater detail below.

1. Web-based Directory of Capital: The Directory of Capital will assist entrepreneurs to identify and access capital most appropriate to their business and interests. Upon entering the site, the entrepreneur will be asked to complete a short survey, which will result in an individualized list of finance and investment sources of capital being generated, including web-links for more information. Too often, entrepreneurs waste time and energy during their search for capital. This site will build on existing finance and investment websites through collaborative relationships with trade groups, government offices and other nonprofits.

*Status Report:* The framework for the Directory of Capital has been developed and the private equity portions have been detailed. We are in the preliminary stages of acquiring partners to build out the debt portions of the site. A prototype of a small business page for all legislators has been developed and could be used to host the directory, as well as other resources for small businesses. The initial launching strategy includes a number of regional events held in conjunction with local business journals.

2. Dictionary of Community Development Terms: Establishing public/private partnerships can be challenging, especially in new investment areas. Having a common language can help. In 1995, the California Community Economic Development Association (CCEDA) prepared its first dictionary and resource guide for community development practitioners and funders. It was then updated in 2002 to reflect new approaches to revitalizing historically underserved neighborhoods and businesses, including new concepts related to "individual asset building" and "smart growth."

*Status Report:* CCEDA is again in the process of updating its directory, including the incorporation of new finance and investment terms and concepts. The Advisory Group will be serving as an advisor to this update to ensure that investment concepts relating to emerging domestic markets and the important roles of community and financial intermediaries are appropriately included.

3. Regional Investor Workshops: As discussed earlier, several public pension funds have already adopted emerging domestic market and emerging manager investment policies and programs. A top priority for the Advisory Group has been to increase capital to small, emerging, and fund-to-fund investment strategies. This focus should lead to greater diversity of asset managers and ultimately to greater diversity of business owners. A conservative estimate is that over \$11 billion has been targeted nationally for investments in emerging domestic markets, at least \$3 billion of which is still available to appropriate investment opportunities in California. Of the moneys that have been invested, there are still partnership and collaboration opportunities which could be developed to enhance private investment in the state's more diverse communities and business enterprises.

*Status Report:* Planning is underway for the first of several investor roundtables where smaller EDM investment firms and emerging managers can meet with the four larger EDM funds that have been hired to deploy CalPERS, CalSTRS, LACERS, and LACERA moneys. The initial roundtable is scheduled for the early summer and will be hosted by the Dean of the Business School at California State University, Fresno.

### **Section III - Recommendations for Further Actions**

This section includes a list of actions that can be undertaken by the state to enhance the development of California's emerging domestic markets.

1. Increase Focus on Emerging Domestic Markets: The significant demographic shifts in California's population pose important economic challenges and opportunities for the state. There is a need for a sustained and coordinated effort by the Legislature to study issues related to California's emerging domestic markets, including the development of an effective path forward and the network of stakeholders ready to accomplish the task.

*Proposal:* Sponsor a resolution calling for the establishment of a Joint Legislative Blue Ribbon Commission on Emerging Domestic Markets. Among other items, the Commission should explore how private investment can best be leveraged through the strategic realignment of public programs, effective models for engaging California's public and private institutions of higher education in supporting entrepreneurs, and how a state debt and equity fund could advance private equity investment in historically underserved areas. *Status:* Resolution establishing the Commission has been drafted and awaits introduction.

2. Increase Scale in Public Debt Markets: New financial products need to be developed to address the capital needs of emerging businesses. As a first step, the state should examine how it could help aggregate state guaranteed loans into salable securities for the purpose of establishing a viable secondary market.

*Proposal:* Require the California Small Business Board to examine new financial products that could be derived through the innovative use of existing state resources. The examination should include, but not be limited to, the aggregation and sale of loan guarantees under the state Small Business Loan Guarantee Program. The Board should engage the foundation, nonprofit, finance, and investment communities in its review to enhance market acceptance of subsequent financial products. *Status:* AB 2416 (Fuentes) has been introduced.

3. Track Existing CRA Capital: The federal Community Reinvestment Act requires banks to annually report and demonstrate progress toward serving people in lower income communities. Large bank mergers and acquisitions may be approved in conjunction with specific community reinvestment commitments. Identifying and tracking these commitments can be challenging. The state should facilitate the

dissemination of this information and, thereby, allow the free market to help implement these commitments in the most efficient manner.

*Proposal:* Require the Business, Transportation, and Housing Agency, or one of its departments, to track significant commitments made by federal and state chartered banks related to community reinvestment. The information could be shared through the existing agency website and outreach to local and regional economic developers and financial institutions. *Status:* AB 1418 (Arambula) will be amended to include these provisions.

4. Build Core EDM Databases: A thorough quantitative analysis of emerging domestic markets is inhibited by a lack of good data. In addition, community leaders are interested in knowing more about the effects of these types of investments on community development but lack a common set of metrics to set baselines and measure impacts. Although major initiatives have been launched by community development organizations and foundations to help bring together a national database, data bases remain fragmented and often insufficient in size, scope, and/or format. The state could facilitate the maturing of this investment space by helping to establish a public/private consortium to host a nonproprietary database.

*Proposal:* Establish an EDM Data Consortium for the primary purpose of collecting and making data available to further the development of emerging domestic markets, including, but not limited to, information related to emerging domestic market firms and industry sectors, financing data on debt and equity, and metrics used in measuring non-financial performance. The consortium would be responsible for establishing appropriate protocols to monitor accuracy, set standard definitions and terms, and establish formats for data submittal. The consortium should also be responsible for ensuring privacy rules and best practices are enforced at all times. *Status:* AB 2636 (Arambula) has been introduced.

5. Maximize Existing Entrepreneurial Opportunities: The state and federal governments offer a variety of programs and services to assist businesses, with a special emphasis on early-stage and small business development. The state could more effectively deploy these programs by identifying programs and services in a manner that more appropriately matches private investment activities, i.e. early-stage capital, resources to enhance management literacy, and funding for employee training. As a first step, JEDE prepared a special catalog of state economic and workforce development programs. This catalog is available at [www.assembly.ca.gov](http://www.assembly.ca.gov) under JEDE Committee Website. This catalog, currently organized by agency, could be redrafted to present state and federal programs and services as parts to a comprehensive entrepreneurial technical assistance and capital support strategy.

*Proposal:* Develop an Entrepreneurs' Catalog of public programs, including, but not limited to, sections on programs and resources available to assist business owners to develop their initial business plan, obtain financial or technical assistance in training employees, and finding seed and early-stage debt and equity capital. *Status:* The JEDE Catalog of State Programs will be redrafted.

6. Improve Access to Existing Entrepreneurial Funds: The state has no coordinated method for announcing the availability of economic, business, and workforce development program moneys. While the state advertising and outreach methods may seem sufficient by other public sector stakeholders, many businesses find our government websites confusing and poorly organized. Making existing opportunities more readily understood would benefit the state, as well as local businesses.

*Proposal:* Establish a one-stop web location where entrepreneurs can find a comprehensive listing of funding opportunities related to state procurement, economic development, and workforce investment. The site should include a clear description of the programs and services, including links for eligibility and application procedures. *Status:* AB 2854 (Mendoza) has been introduced.

## **Section IV - Future Work on Emerging Domestic Markets**

This report has provided information on the first four months of the Advisory Group. While the Advisory Group has made good progress, many issues remain to be addressed in order for our goal of a fully functioning sub-asset class of private equity to be realized.

This first round of Advisory Group meetings focused on how to increase an individual business's access to capital, especially private equity capital. In our next round of meetings, we will begin to examine real estate and infrastructure investment practices, as well as investigate ways to strengthen the capacity of local finance and community intermediaries to be an effective link between institutional capital and local businesses and communities.

Ultimately, investment strategies must target both the individual business and the community in which it is located. Failing to achieve both will result in businesses leaving the area, either because they can no longer afford the rents or because they are too successful to remain in the "poor area of town." By combining community development and business development investment strategies, true neighborhood transformation can be achieved. A key role in this transformation can be played by the financial and community intermediaries.

## **Appendix**

### **Members of the Advisory Group**

The Advisory Group was convened in conjunction with the California Legislature's Latino Caucus and in cooperation with the California Hispanic Chambers of Commerce. The Advisory Group Executives represent leaders in the financial and economic development community.

Our facilitators included, Toni Symonds, Chief Consultant to JEDE, and Paul Garza, independent business consultant and member of the Access to Business Capital Committee of the California Hispanic Chambers of Commerce. Technical assistance and guidance was also provided by CalPERS and CalSTRS, who continually demonstrated their commitment to find new financially viable methods to get institutional capital into emerging domestic markets.

#### *Advisory Group Executives*

**Mr. Mujahid Abdullah**

Sustainable Capital  
Investment Banker

**Mr. Chris Ailman**

California State Teachers Retirement  
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**Ms. Penelope Douglas**

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California Hispanic Chambers of  
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