ECONOMIC INNOVATION GROUP

Challenges and opportunities in access to capital and new business formation

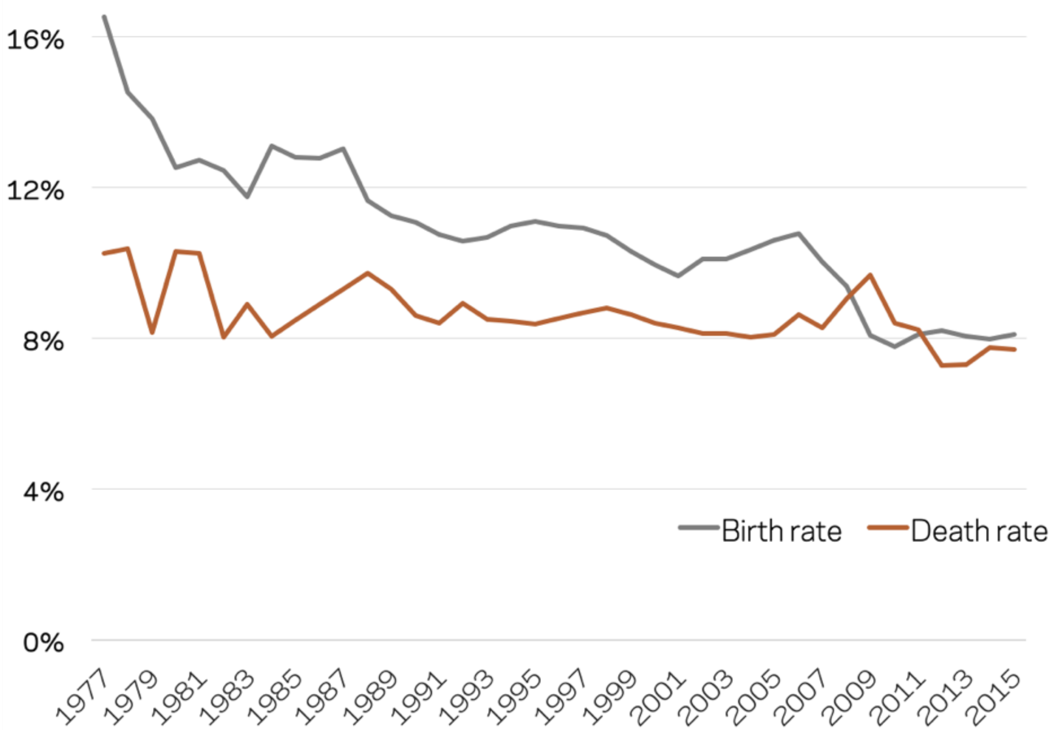
Kenan Fikri, Director for Research

ECONOMIC INNOVATION GROUP / Washington, DC / @kenanfikri

The rate at which Americans create businesses has tumbled

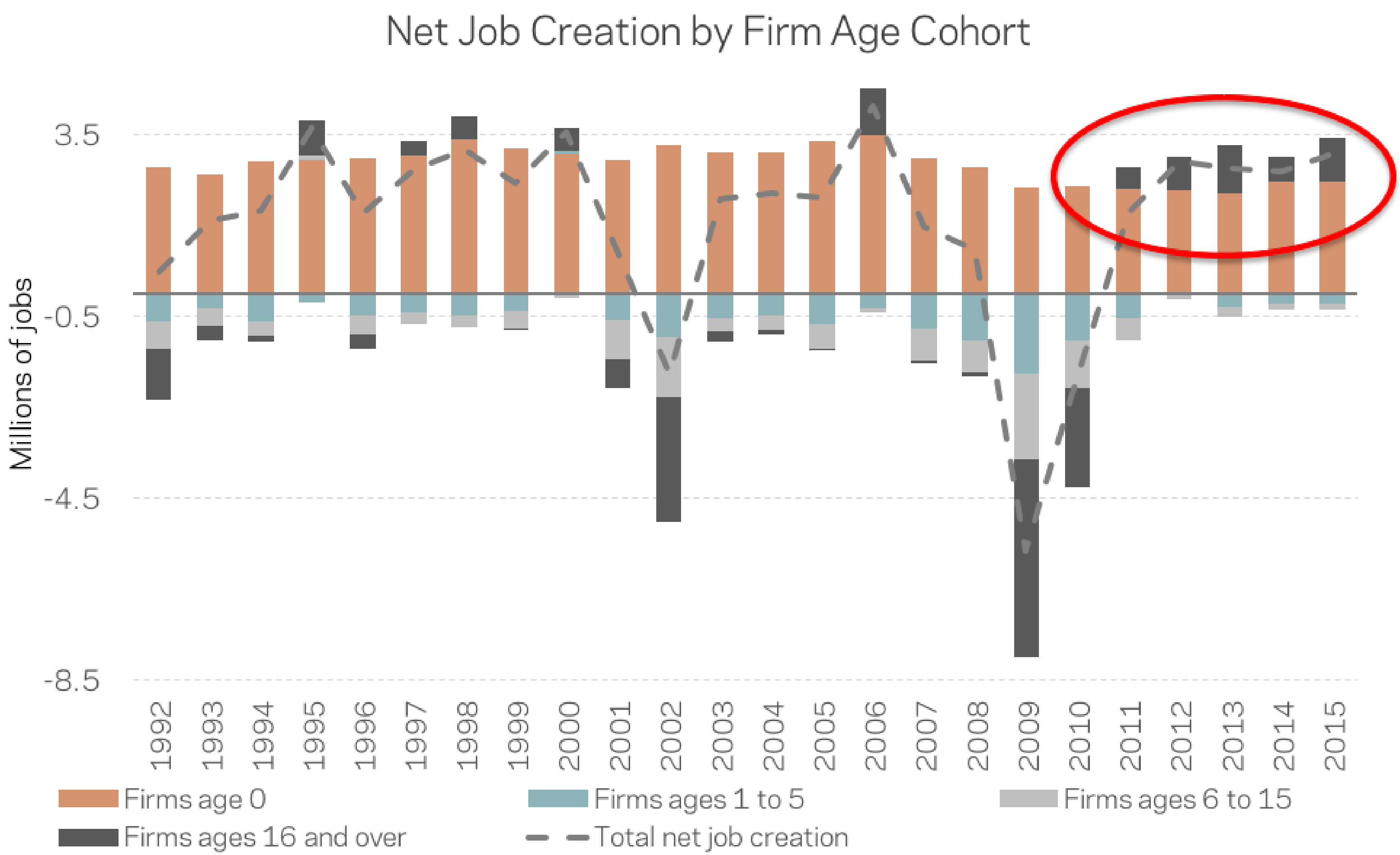
- During the past 40 years, the startup rate has halved.
- The United States is missing about 100,000 company launches a year right now.
- The development is a mix of long-term, secular trends and the aftereffects of the Great Recession.

New firm startup and existing firm closure rates



Source: U.S. Census Bureau's Business Dynamics Statistics

Incumbents are eating away at new businesses' historical primacy in net job creation.



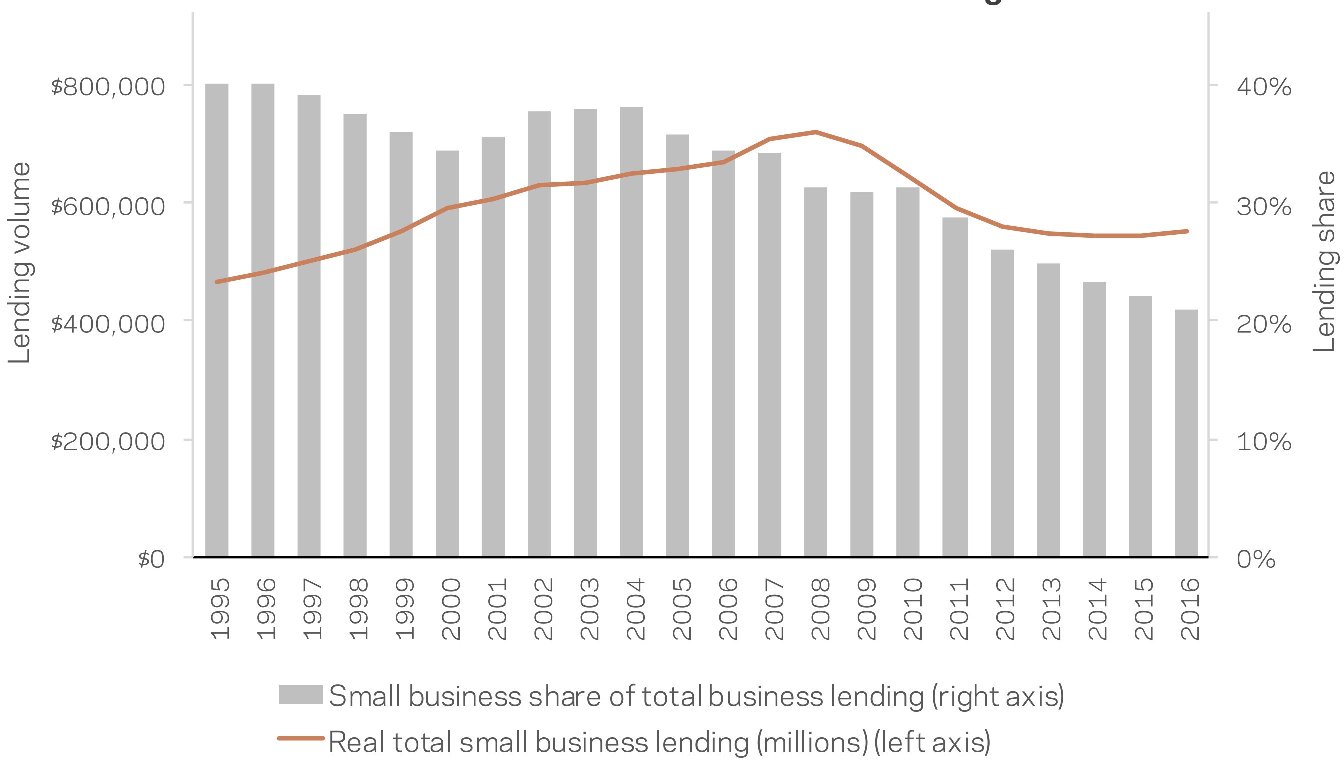
EIG

Source: U.S. Census Bureau's Business Dynamics Statistics

Banks have retreated from small business lending, leaving a financing void for new and many smaller existing firms alike.

- Meanwhile three-quarters of all U.S. venture capital flows to only three states: CA, MA, and NY.
- The number of community banks, integral to local business networks, has declined by a quarter over the recovery.
- Across the banking sector, 1,700 branches closed last year—the largest decline on record.

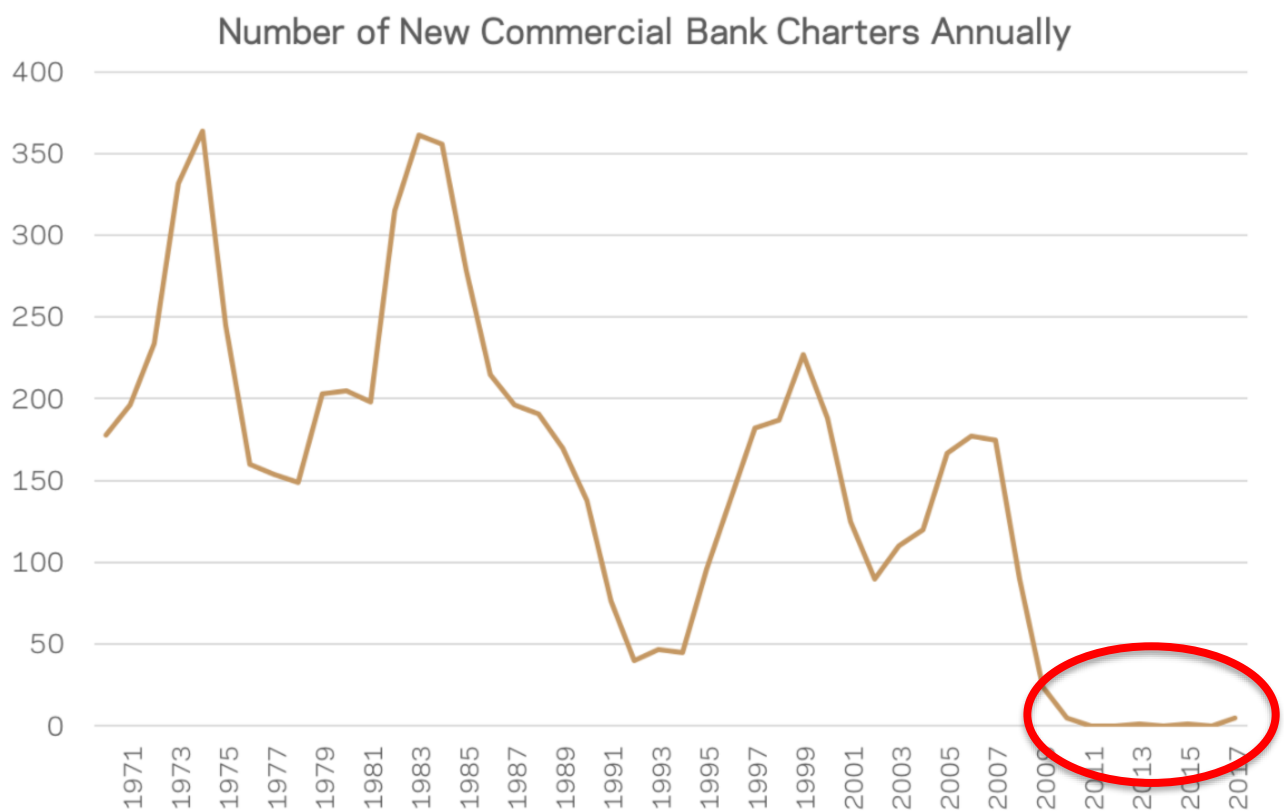
Trends in Small-Scale Business Lending



Source: FDIC

Startups in the banking sector are essentially extinct.

- From 2011 to 2016, only two new commercial banks were chartered in the United States, compared to an annual average of 177 from 1966 to 2007.



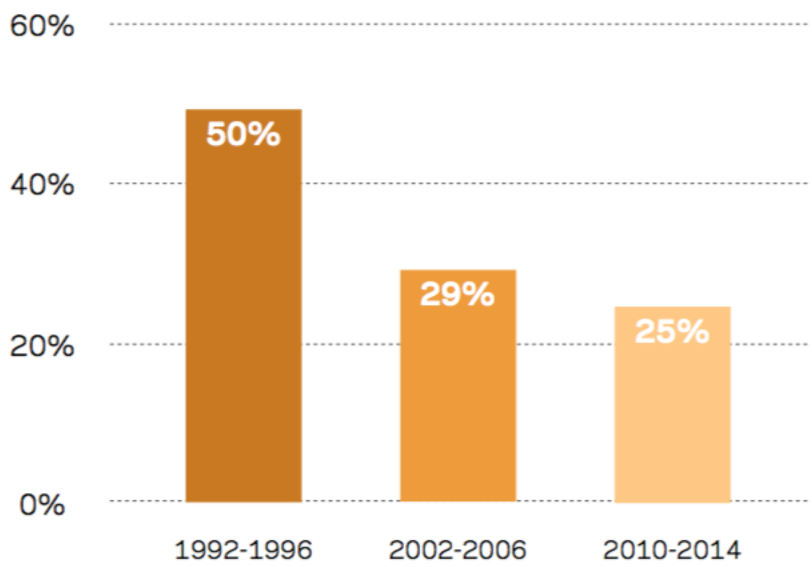
Source: FDIC

This slow winding down of the economy's dynamism is producing more *geographically* unequal outcomes.

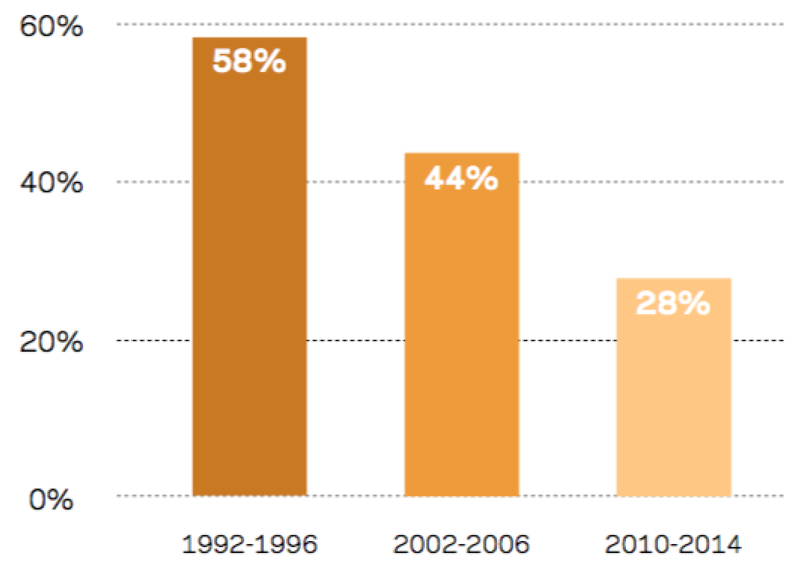
- In the 1990s, half or more of all counties grew at the national rate. Now only one quarter do.
- National figures are becoming less reflective of local realities.

Share of U.S. counties matching the national rate of growth

Business establishments



Employment



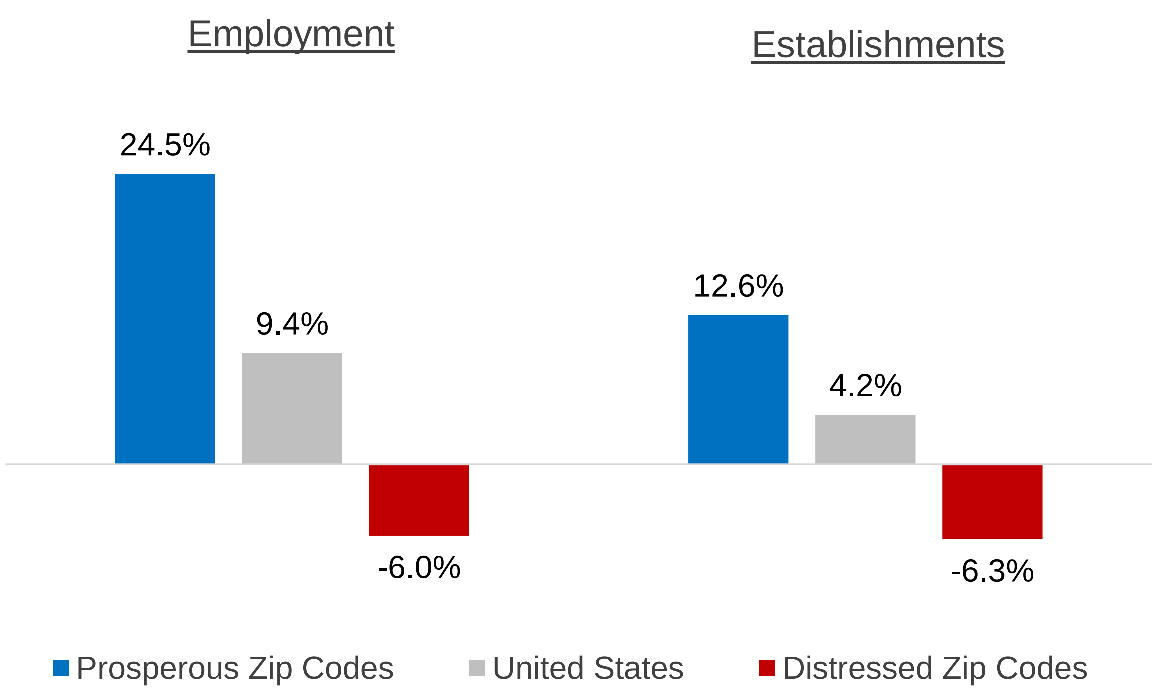
EIG

Source: U.S. Census Bureau's County Business Patterns

Job and business growth fails to reach most distressed zip codes.

- More than half of the country's distressed zip codes contained **fewer jobs and places of business in 2015 than they had *in 2000***.

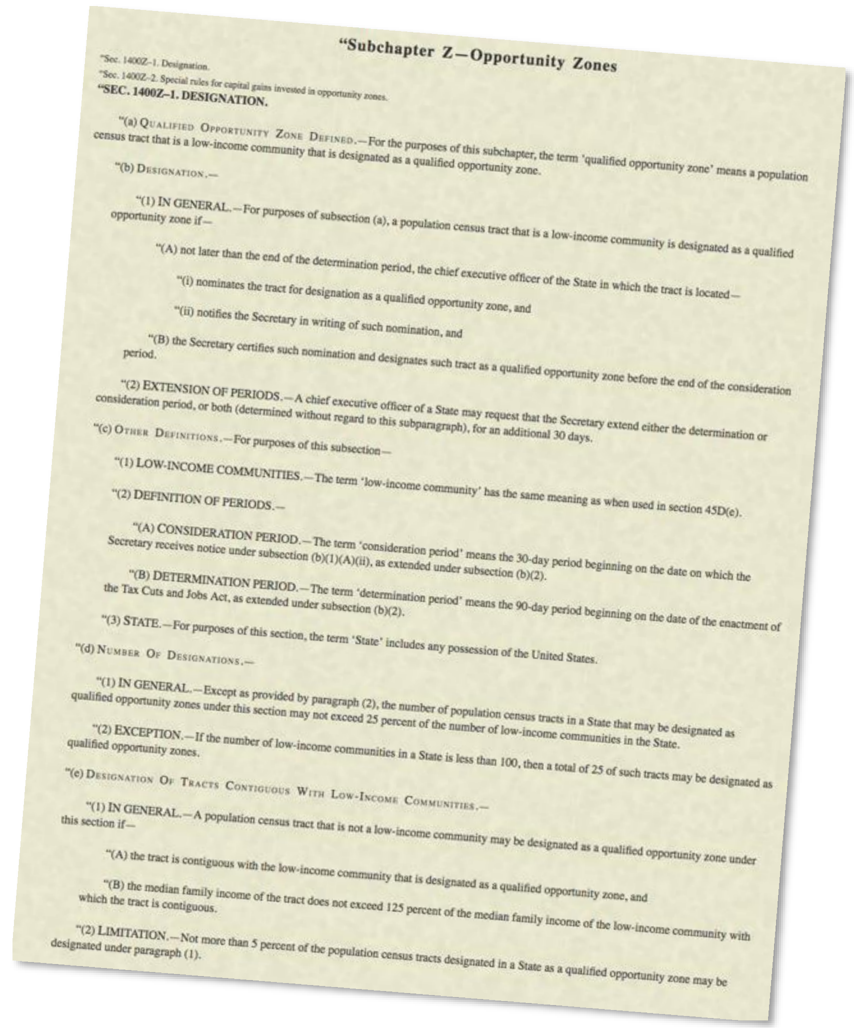
Average 2011-2015 Growth Rates



Source: EIG's Distressed Communities Index; U.S. Census Bureau

Opportunity Zones are a new, bipartisan solution to expand the geography of economic growth.

- The Opportunity Zones provision is designed to **spur long-term private sector investments** in low-income communities nationwide.
- This new economic development program offers a frictionless way for investors to **reinvest unrealized capital gains** into distressed communities through Opportunity Funds, in exchange for a graduated series of incentives tied to long-term holdings.
- It is the first new national community investment program in over 15 years, and has the potential to **scale** into the largest economic development program in the U.S.
- It is specifically designed to channel more **equity capital** into overlooked markets.



"Subchapter Z—Opportunity Zones

"Sec. 1400Z–1. Designation.
"Sec. 1400Z–2. Special rules for capital gains invested in opportunity zones.

"SEC. 1400Z–1. DESIGNATION.

"(a) Qualified Opportunity Zone Defined.—For the purposes of this subchapter, the term 'qualified opportunity zone' means a population census tract that is a low-income community that is designated as a qualified opportunity zone.

"(b) Designation.—

"(1) IN GENERAL.—For purposes of subsection (a), a population census tract that is a low-income community is designated as a qualified opportunity zone if—

"(A) not later than the end of the determination period, the chief executive officer of the State in which the tract is located—

"(i) nominates the tract for designation as a qualified opportunity zone, and

"(ii) notifies the Secretary in writing of such nomination, and

"(B) the Secretary certifies such nomination and designates such tract as a qualified opportunity zone before the end of the consideration period.

"(2) EXTENSION OF PERIODS.—A chief executive officer of a State may request that the Secretary extend either the determination or consideration period, or both (determined without regard to this subparagraph), for an additional 30 days.

"(c) Other Definitions.—For purposes of this subsection—

"(1) LOW-INCOME COMMUNITIES.—The term 'low-income community' has the same meaning as when used in section 45D(e).

"(2) DEFINITION OF PERIODS.—

"(A) CONSIDERATION PERIOD.—The term 'consideration period' means the 30-day period beginning on the date on which the Secretary receives notice under subsection (b)(1)(A)(ii), as extended under subsection (b)(2).

"(B) DETERMINATION PERIOD.—The term 'determination period' means the 90-day period beginning on the date of the enactment of the Tax Cuts and Jobs Act, as extended under subsection (b)(2).

"(3) STATE.—For purposes of this section, the term 'State' includes any possession of the United States.

"(d) Number Of Designations.—

"(1) IN GENERAL.—Except as provided by paragraph (2), the number of population census tracts in a State that may be designated as qualified opportunity zones under this section may not exceed 25 percent of the number of low-income communities in the State.

"(2) EXCEPTION.—If the number of low-income communities in a State is less than 100, then a total of 25 of such tracts may be designated as qualified opportunity zones.

"(e) Designation Of Tracts Contiguous With Low-Income Communities.—

"(1) IN GENERAL.—A population census tract that is not a low-income community may be designated as a qualified opportunity zone under this section if—

"(A) the tract is contiguous with the low-income community that is designated as a qualified opportunity zone, and

"(B) the median family income of the tract does not exceed 125 percent of the median family income of the low-income community with which the tract is contiguous.

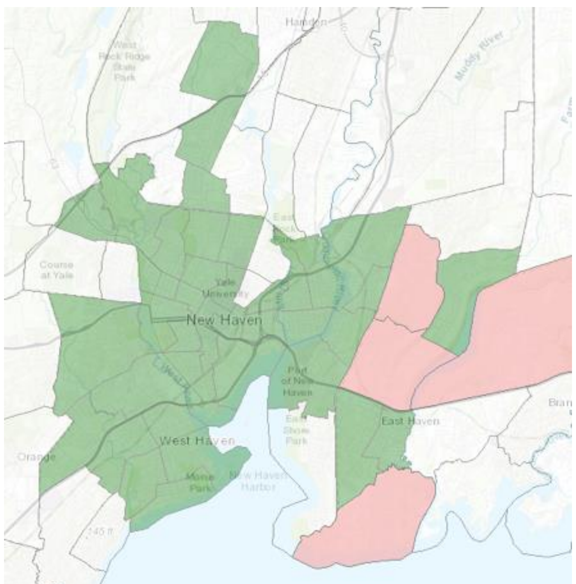
"(2) LIMITATION.—Not more than 5 percent of the population census tracts designated in a State as a qualified opportunity zone may be designated under paragraph (1).

EIG

What do local leaders need to know about the provision?

There are three major components to Opportunity Zones:

Zones



Funds

Investments

What will this look like on the ground?

Unlocking access to capital for **entrepreneurs**

LaunchTennessee

Helping **innovation districts** deliver on their promise

Improving the economics of **brownfield** redevelopment

There are three stages of next steps for local leaders

1. Zone Designation (immediate)

- Work with your state counterparts to **provide local market intelligence** so that your region's highest priority, opportunity, and need census tracts get included in your state's nominations. Hold your state elected representative to account for holding bottom-up consultations.

2. Setting up Funds (2018)

- Raise awareness about the program among local banks, financial institutions, investors, and business networks to **encourage the establishment of Opportunity Funds** specializing in your state or region.

3. Facilitating investment (on-going)

- Raise awareness about the program now **with local entrepreneurs** and high-growth companies that may be eligible for investment from Opportunity Funds.

- Work with universities, startup incubators and accelerators, and other **ecosystem partners** to ready your home region to take advantage of the program.

- Work with local planners and developers to determine how this new financing model can integrate with existing or anticipated **development or infrastructure plans**.

- Liaise actively with local, regional, and national funds to make sure they are **aware of eligible investment opportunities** in your region.

Visit **eig.org/opportunity zones** for more information

EIG brings together leading entrepreneurs, investors, economists, and policymakers from across the political spectrum to address America's economic challenges.

WEB eig.org EMAIL kenan@eig.org

facebook.com/EconomicInnovationGroup

linkedin.com/company/economic-innovation-group

twitter.com/InnovateEconomy

EIG