

Charlotte May Have Cracked the Code on Affordable Housing. Here's How

A \$58 million fund is being used to buy up affordable buildings and keep the rents low.

By Nate Berg, Fast Company, January 25, 2021

The Lake Mist apartment complex in Charlotte was in danger, and so were its residents. A cluster of two story brick-and-tan buildings near a busy commercial corridor, the 144-unit complex was one of a dwindling number of rental options available to residents making less than the area's median income. It's not a public housing development or an official affordable housing project, but Lake Mist, with rents starting around \$600 per month, is, de facto, part of Charlotte's affordable housing stock. But its rents weren't likely to stay so low for long, and real estate investor Mark Ethridge wanted to do something about it.

"Rent in this [neighborhood] had increased 34% since 2015," says Ethridge, a partner at local firm [Ascent Real Estate Capital](#). "And two of the apartment complexes next to this one had recently been bought by what I would deem value-add private equity." Displacement of the residents at Lake Mist was only a matter of time.

Ethridge had watched for years as properties like this were snatched up by big money investors who'd quickly renovate them, jack up the rents and then sell them off for a quick profit. With an estimated 120 people moving to the city every day and an economy on the rise, growth in Charlotte had put these kinds of apartment complexes in the sights of housing investors who saw them not as affordably priced homes for lower income residents but as undervalued assets.

But Ethridge had an unusual solution: he wanted to buy the property, fix it up, and keep the rents affordable through a 20-year deed restriction that places legal rules on how the property can be used and priced. Knowing the demand for this tier of housing and the small but steady returns they could provide, Ethridge saw apartment complexes like Lake Mist as long-term plays. They'd provide a slow and reliable return, with the added benefit of helping to combat the city's affordable housing shortage.

These types of complexes on the private market—known as naturally occurring affordable housing, or NOAHs—were both endangered and easy pickings for an investor looking to turn a small profit while making a difference. But Ethridge and his firm could only do so much on their own. In partnership with a group of mostly local organizations and two of the city's most prominent investors, they've built up a \$58 million pool of money called the Housing Impact Fund, dedicated specifically to buying these kinds of properties and preserving them as affordable housing. The fund closed on Lake Mist in December. If their plan works, they could be crafting a new and profitable model for dramatically increasing the amount of affordable housing in Charlotte and beyond.

In the world of for-profit real estate investment, the Housing Impact Fund's focus on naturally occurring affordable housing is as straightforward as it is unconventional. It's not the first to make NOAHs a priority, though. The approach has been tried, in various forms, in other cities around the U.S., including [Minneapolis](#), [Washington, D.C.](#) and [Austin](#), typically as a consortium of public and private sector actors aiming to help provide much needed affordable housing.

Moha Thakur, policy associate at the [National Housing Trust](#), a national nonprofit focused on preserving affordable housing, says NOAH investments are powerful but rare. "Most investors are probably hoping to receive a rate of return that is higher than what is generated by affordable housing, which poses a problem for developers who are trying to seek out funding but also maintain some level of affordability," she says. Compared to for-profit real estate investments with [returns upwards of 15%](#), the return on investment in naturally occurring affordable housing is typically in the single digits.

The housing market is often bifurcated into two groups: profit-seeking private developers with big budgets and mission-driven affordable housing developers dependent on limited financing options like the [Low Income Housing Tax Credit](#). "What the market sometimes lacks is something of a combination of the two, a developer with experience in the unsubsidized housing but with the dedication to maintain good quality long term affordable housing," Thakur says.

The challenge, she notes, "is finding the right investors who are willing to accept a lower rate of return so that the property can maintain its long-term affordability but remain as good quality housing."

A Charlotte native with a long family history in local journalism, Mark Ethridge had been working in the city as a loan originator, helping real estate investors line up financing to buy commercial properties. By around 2015, after the worst effects of the recession had tapered off, Charlotte was growing and formerly fringe areas of the city were becoming urban. A light rail line, opened in 2007, had [spurred more development](#) along one of the city's main corridors, and the city's population has [grown by more than 100,000](#) over the past decade. Ethridge found himself working with clients on the financing for a lot of older, low-rent apartment complexes—overlooked properties that were seeing renewed interest as the city's population swelled.

"It occurred to me that the vast majority of people who make less than median income who live in rental housing live in private unrestricted properties," he says. "So I got really curious about what folks were doing to maintain affordability at these properties."

He made a database of every single apartment complex in the city that was built before 1990, including who owned, how much they bought it for, and what they were charging for rent. The database soon had more than 20,000 units worth of housing within a few miles of downtown.

“Lo and behold, what I found was these properties were slowly changing hands,” Ethridge says. Private equity firms, often from outside Charlotte, were behind many of the sales. From years inside the business, he knew this was likely to lead to displacement. “The way you make money in real estate traditionally is you buy something, you increase the rent and then you sell it,” he says. “So all of that is a recipe for bad outcomes for residents.”

In 2017, Ethridge joined a [task force](#) at the nonprofit economic and cultural development organization [Charlotte Center City Partners](#) focused on finding solutions to the city’s affordable housing shortage. He focused on researching the preservation of NOAHs, looking at what cities like Minneapolis and Austin had done. Though the city of Charlotte had an affordable housing bond that was regularly reapproved by voters, it focused primarily on new construction—an important source of housing, but one that was slow to materialize, often taking three to four years from proposal to ribbon cutting. “We weren’t really thinking about this whole bed of thousands and thousands of older apartment units that really serve as a backbone for affordable housing in cities like Charlotte,” Ethridge says.

Around this time, he left his lending job to work with one of his clients, Ascent Real Estate Capital. “When I joined the company, I said I want to start buying old apartments, and when we buy them I don’t want to raise rents,” Ethridge says. “And my partners were like, ‘Uh, OK. Go figure it out.’”

The city’s affordable housing bond, a tax-funded pool of money dedicated to financing housing projects, had recently been increased from a biannual \$15 million to \$50 million, and was amended to include provisions not just for new build projects but also preservation. Ethridge saw an opportunity to tap into that financing to start buying NOAH properties. He raised some equity and made his first purchase in 2019, what he calls a “bite-size deal” for a 98-unit apartment complex in southeast Charlotte. To secure the affordable housing financing from the city, Ethridge structured the deal so that the property would maintain specific levels of affordability for 80% of the units, based on the area median income. Through a deed restriction lasting 20 years, these would be priced for residents making between 30% and 80% of this average income level, creating rents equivalent to about \$400 or \$600 a month in a market where prices were closer to \$900. The complex would stay at affordable levels for families making as little as \$20,000 a year and still provide its investors a modest return.

With that deal, the city of Charlotte suddenly had nearly 100 new long-term affordable housing units. But in a city short tens of thousands of units of affordable housing, bite-size deals would only do so much.

“We always knew that we needed a source of capital that could scale this,” Ethridge says. “To really make an impact you need to buy a thousand units or more. We’re talking about tens of millions of dollars of equity.” It was money Ethridge didn’t have. He just needed the right partners who could help find it.

Nelson Schwab and Erskine Bowles have been friends since college, through long and prominent careers in Charlotte and beyond. Schwab was a longtime executive in the theme park business and co-founded a [private equity firm](#) with Bowles in Charlotte in the 1990s that's managed more than \$2 billion of investments in the Southeast. Bowles is the former president of the University of North Carolina system, and previously served as the chief of staff to President Bill Clinton. Now in their 70s, the two are the kind of public figures who have the clout and experience to make a difference in their city.

Schwab and Bowles shared concerns about the rising homelessness in Charlotte and were looking for a way to chip away at the problem. People told them that if they really wanted to have an impact, they needed to address the shortage of affordable housing.

"The more we heard about the traditional way of creating affordable housing, the less we liked it. It was very government centric, the economics were very tough, it took three or four years to deliver a project," Schwab said in a recent video call. "You can see from the monitor here, we're not young guys, so we wanted to get moving quickly and get this thing going."

But the cost of buying land and building new affordable housing where it was needed – near transit and jobs – was too high in the growing city. "The math didn't work," says Bowles. "So we tried to think of a way to get involved where the math would work."

It was late 2019, and they learned about NOAHs and Ethridge's first deal, closed just a few months before. And with his database showing more than 20,000 units of possible NOAH housing in and around the city center, they saw the potential of what he was doing to help solve the problem. "We felt good that if we raised money, we'd have a place to spend it," Schwab says.

In early 2020, Schwab and Bowles started structuring the financial side of things to ensure both long-term affordability and steady returns to investors, settling on an approach that would generate about an 8% return – more like investing in a bond than a stock, Ethridge says. They started making calls – more than 125, by Schwab's estimate – and raising money. They soon had \$58 million committed from investors like the bank [Truist Financial](#) and the hospital system [Atrium Health](#) and created what they've named the Housing Impact Fund. They could have raised even more. "We actually cut it off at \$58 million because we were tired of fundraising and we were ready to get it going," Schwab says.

Bowles insists this is not philanthropy, and giving the fund a for-profit structure was a way to bring the discipline needed to ensure it would work for the long run. "We are capitalists," he says. "We believe in capitalism. But if it's going to survive, we have to make it work for more people. A lot more people."

Charlotte was in need of this kind of help. In 2015, a landmark [study](#) came out of Stanford University's Center on Poverty and Inequality analyzing intergenerational

wealth and economic mobility in cities across the country. Of the 50 cities ranked in the report, Charlotte came in dead last.

“It determined that if you were born in the '80s in Charlotte, your chance of growing out of poverty as an adult was kind of slim to none,” says Pamela Wideman, director of Housing and Neighborhood Services at the City of Charlotte. She says it’s impossible to de-couple the lack of affordable housing from that statistic. Stable and affordable housing is key to creating the kind of self-sufficiency lower income families need to get themselves and their children on steady footing, she says.

The Stanford report put that need in stark light. “That was a big surprise to the white community here because Charlotte’s growing like a weed, we’re creating jobs every day, the business community is bustling,” says Bowles. “But it wasn’t a surprise to people in the Black and brown community in Charlotte.”

In the election after the report, the \$50 million housing bond was easily approved. In 2020, voters backed the bond again. The city has committed to supporting the efforts of Ethridge and has already used some of its affordable housing bond money to help finance the Housing Impact Fund’s first investment. “We want to help people stay in place and we don’t want to lose that supply of affordable housing,” says Wideman.

The fact that Ethridge is from Charlotte is also important, according to Wideman, who worries that too many outside investors buying up the city will give Charlotte less control over its future.

But investing in NOAHs is not the only solution. “I won’t say that the preservation is better than new construction,” Wideman says. “What I will say of the preservation is it makes sure that the existing housing is kept up to par with the new. It makes sure people can age and stay in place, so they don’t have to worry about somebody coming in and buying their property, tearing it down, developing it into luxury and they can never afford to be back there.”

In addition to new construction, Ethridge’s focus on preserving the affordably priced apartments on the private market is becoming part of the city’s affordable housing strategy, and other affordable housing developers are getting in on the effort. The Charlotte office of Local Initiatives Support Corporation, a national nonprofit focused on community development, is now investing in NOAH properties alongside Ethridge and the Housing Impact Fund. According to LISC Charlotte executive director Ralphine Caldwell, preserving these properties as affordable housing will be instrumental in reversing the housing and homelessness problems in the city. “If we had just focused on new build, we would not be moving the needle,” she says.

The Housing Impact Fund’s first purchase, Lake Mist, cost \$18.5 million, including about \$4 million in financing from the city. With the \$58 million Schwab and Bowles helped raise, the fund is targeting investment in around 1,500 units over the next two years, and Ethridge says several deals are currently in the works. Each property will have the

same 20-year deed restriction, with 80% of units set aside for households earning less than the area median income. And in another innovation, Ethridge worked with officials in Charlotte and Mecklenburg County to craft a workaround for their property taxes – a requirement due to the fund’s for-profit status – which will use whatever they owe each year to fund a housing rental subsidy for very low income residents.

“A lot of city councils don’t like to mess with their property taxes because that truly is their bread and butter for funding city services,” says Wideman, from the City of Charlotte. “But you’ve got to be willing to try things.”

As part of Schwab and Bowles’ effort to make capitalism work for a broader spectrum of people, they added a clause to the Housing Impact Fund’s structure requiring that at least 80% of the rehab work and construction on its investment be done by minority contractors.

Ethridge calls the effort “social impact capital,” and he says the Housing Impact Fund’s investors recognize that their investment can be both beneficial to society and profitable. “The nice thing about buying existing properties, unlike new construction, they cash flow the day you buy them,” Ethridge says. “So we will pay quarterly returns to our investors and we expect that cash flow to be relatively consistent.”

And 20 years down the line, when the deed restrictions expire, the affordable housing doesn’t necessarily disappear. The fund has another clause that requires any sales to divert 60% of profits to another fund for affordable housing. “We aren’t just solving this problem for 20 years,” Bowles says. “We’ve had calls from people all over the country who’ve heard about what we’re doing and think can we do this in our city. We’ve been very candid about this, that if this works here in Charlotte we’re going to raise another fund, and then another fund after that.”

Key to making the fund work, Bowles says, is Ethridge. “While he’s got a heart as big as this room I’m sitting in, and a desire to do the right thing, and a belief in helping these people that need the help, he’s also realistic, practical and effective,” he says. “I think he’s truly an extraordinary person.”

Ethridge sees the work as simply meeting a need that wasn’t being met by the old way of building affordable housing. “Altruism and philanthropy can’t be the only venue for us to solve our problems,” he says. “We need all the financial discipline, all the entrepreneurship, all the expertise the private sector can bring and find a way to do altruistic things. We think this is a healthy balance of that.”