AN INVESTMENT LETTER FOR MINNESOTA PHILANTHROPISTS

July 15, 2006

The remarkable success of the Neighborhood Development Center in nurturing the development of startup businesses in economically challenged neighborhoods is the focus of this Investment Letter. One of the Twin Cities best kept secrets has been the hidden reservoir of business talent that exists in the region. Mike Temali and the NDC have learned how to identify, train, advise and assist in the financing of these self styled entrepreneurs.

The philanthropic investor can deliver new tax revenue that equates to a return of 25% annually to the community after breakeven is achieved shortly after the end of the fourth year. In terms of the volume of business generated byNDC client businesses Wilder Research concluded that $12.00 of business activity were returned to the neighborhood for every $1.00 invested by the Neighborhood Development Center.

WHAT'S THE PROBLEM?

- The development of major regional commercial and retail centers outside of urban residential neighborhoods has put traditional neighborhood small businesses at a competitive disadvantage.
- While beneficial in many ways these events have removed much of the traditional leadership as well as the "walk to work" life style of the past from the urban core.
- When the legitimate and neighborhood sensitive businesses leave the community potential is ripe for gradual economic deterioration and the emergence of an unhealthy sub-culture that decides to earn its living any way it can.
- What often results are concentrations of poverty, deteriorating schools, increased rates of crime and continued exodus of middle class residents to more attractive neighborhoods.
- The Minnesota taxpayer winds up footing the bill for a host of social services and criminal justice system responses that result. The quality of life for the remaining residents declines. Minnesota's workforce of the future is harmed by the young people who fail to develop to their full potential.

HOW DOES THE NEIGHBORHOOD DEVELOPMENT CENTER HELP?

- Through neighborhood surveys NDC identifies potential entrepreneurs who may be operating micro enterprises out of their homes and who have the work ethic, technical skills and business ideas to start, maintain and grow a business.

- Micro-entrepreneur training is conducted in small classes with participants all from the same community. This creates a peer group that provides encouragement and support to one another as they explore becoming business owners.

- For many start-up businesses traditional funding sources is not an option. After successful completion of the NDC micro-entrepreneur training class, loans are available up to $10,000 for start-up businesses and up to $50,000 for growing businesses.

- In order to help entrepreneurs respond to changes and new challenges NDC provides experts to consult with business owners. More than 4,000 hours of technical assistance is provided each year.

- The lake Street Business and Career Center assists low and moderate people in South Minneapolis by offering entrepreneur training, financing and technical assistance; workforce training and job placement and in addition college admission to Minneapolis Community & Technical College.

- Real estate developments such as the new Midtown Global Market in the former Sears building will house over 62 businesses including start-ups and existing businesses owned by NDC training class alumni. This type of clustering offers new business owners easy access to the full range of NDC services.

WHO BENEFITS?

- Twin City neighborhoods gain as new business activity generates jobs and the entrepreneurs managing these businesses bring stability and new leadership to the community.

- Minnesota taxpayers gain as tax revenue generated by these start up businesses more than offsets the cost of the initial investment by the fifth year of business.

- The state’s economy benefits from the multiplier affect of new spending generated by wages, supplies purchased, rents paid and other expenses.

WHAT'S THE RETURN ON INVESTMENT?

Wilder Research conducted a comprehensive study of the Neighborhood Development Center in November of 2005. The analysis covered NDC activity from 1993 to 2004. During this period 2,676 entrepreneurs were assisted with one or more levels of NDC service. Wilder reviewed a list of NGC clients that might be in business. It was determined that 74% were likely to be still in business. This resulted in the conclusion that 301 clients were still in business. Businesses surveyed had an average of 4.4 employees which together with the 301 business owners resulted in 1,622 new jobs being created.

The Wilder study documented that for the period 1993 to 2004 the 301 existing businesses on average generated the following economic activity each year: Rent $1,527,372; Purchased supplies/materials $1,841,160; Payments to subcontractors $1,375,356; Payroll $9,560,700; Payroll taxes of all business owners $753,240 (understated because 58% of all business owners did not report this information) and property taxes paid of $152,600. In total more than $15,000,000 of economic activity on average was generated each year.

Ninety-seven percent of surveyed business owners received training from NDC; thirty-two percent financing and five percent had a location in an NDC incubator. About one – third of participants became involved with NDC in the last two years. One-third received assistance three to five years ago, about one-fifth five to ten years ago and about one-tenth over ten years ago. On average, businesses have been involved with NDC a little over four years.

Therefore for the purposes of computing the return on investment for NDC it is assumed that the $6,503,362 of total program expenses from 1993 to 2004 was spent over a four year period. The next step is to calculate the benefits provided to the Minnesota tax payer over this same period of time. Payroll taxes of $752,000 and property taxes of $152,000 are paid each year. It is assumed that an additional $660,000 in taxes is collected each year from the general economic activity of the 301 businesses (see page four for details). These taxes generated each year total $1,565,000 or a total of $6,300,000 over the four year period the average business has been involved with the NDC.

- **The four year cost of $6.5 million is nearly offset by $6.3 million of tax revenue generated shortly after the end of the fourth year. Each year thereafter generates an additional $1.6 million of taxes or the equivalent of a 25% annual rate of return on the initial investment of $6.5 million.**

It is assumed that while some businesses may fail in future years others will prosper and offset prospective losses. In addition it is nearly impossible to accurately determine taxes that result from NDC spending in the community. The assumptions used appear to be conservative. Also since 58% of all business owners did not report payroll tax information it is likely that the tax contribution for payroll taxes is greatly understated.

CALCULATING THE RETURN ON INVESTMENT

Assumptions:
Cost Per Entrepreneur Served = $2,430
Cost Per Current Business = $21,606
Cost Per Current Job = $4,923

Dollars Returned To Community	3years	5years	10years	15years	20years
Rent ($1.5 mm)	$4.5	$7.5	$15.0	$22.5	$30.0
Purchased Supplies ($1.8 mm)	5.4	9.0	18.0	27.0	36.0
Payroll ($9.6 mm)	28.8	48.0	96.0	144.0	192.0
Subcontractor Payments ($1.4 mm)	4.2	7.0	14.0	21.0	28.0
Total $ Returned	$42.9	$71.5	$143.0	$214.5	$287.0
Other Taxes ($660)*	2.0	3.3	6.6	9.9	13.2
Payroll Taxes ($753m)	2.2	3.8	7.5	11.2	15.0
Property Taxes ($152m)	.5	.8	1.6	2.4	3.2
Total Taxes ($1,565)	$4.7	$7.9	$15.7	$23.5	$31.4

*Other Taxes assumes that Purchased Supplies of $1.8 million, Sub-contractor payments of $1.4 million and Rent paid of $1.5 million each year for a total of $4.7 million in annual expenditures by NDC businesses generate $470,000 in taxes annually equivalent to a rate of 10% (sales tax, individual and business income tax and added real estate taxes). It also assumes that in addition to payroll taxes the $9.6 million annual payroll of NDC businesses generates added taxes of $190,000 annually, a rate of 2%, as the dollars flow through the system impacting sales, income and real estate taxes.

The state of the art must evolve further to include far more tax data than currently available if more precise measures of ROI are to benefit Minnesota investors and taxpayers.

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