

THE FEDERAL RESERVE BANK OF NEW YORK

MAKING MISSING MARKETS INITIATIVE

In broad brushstrokes, a market requires something of value to be produced that is purchased by a buyer. In most cases, those transactions require some sort of connector to help ease the process. Markets spring up all the time (coconuts for bananas as in the famous economic textbook example), but oftentimes they require some nudging and encouragement. For example, the Federal Housing Administration (FHA), introduced the 30-year fully amortizing mortgage in the 1930s to stabilize the housing market during the Great Depression. The Federal Reserve has been a market crafter of sorts for much of its history (e.g., creating the repo market, Section 13.3 liquidity facilities).

The Federal Reserve Bank of New York, through its Community Development function, is curating a conversation on how we might make a missing market that invests in improving the wellbeing of low- and moderate-income places and neighborhoods. This is something the Federal Reserve already does routinely through its role in enforcing the Community Reinvestment Act and its efforts to make sure that the American economy works everywhere and for everyone. There are trillions of dollars already allocated to improve economic opportunities, health, and well-being across many sectors - social services, public welfare, private corporations, entrepreneurs, impact investing - but too often those efforts are uncoordinated and disorganized.

New York Federal Reserve President John Williams described this problem in a recent speech: “Despite the availability of these resources and the good work being done, there is something missing: effective cross-sector interventions are more the exception than the rule. Efforts can often take the form of one-off interventions that lack the adequate dose, duration, or intensity to significantly improve conditions in the community.”¹ The Making Missing Markets initiative is an effort to bring together leaders in those disparate fields and sectors to debate how we can do better; how might we create new business models that attack the roots of multiple problems to improve opportunities and save tax dollars.

What Contributes to Flourishing?

Everyone understands that countless things had to go right for them to navigate their childhoods and arrive in adulthood with the skills they need to thrive. Many of us can point to a teacher, a coach, a minister, our parents, or a handful of friends who helped us in that journey. In other words, many people made investments in us as individuals—as **people**—that helped us grow. And we can all point to aspects of our communities that facilitated this journey too: good schools, parks, recreation facilities and sports programs, quality housing that was affordable, houses of worship, public libraries, clean air and water, etc. In other words, there were **places** that helped us grow too.

We also know that not everyone has the good fortune to have these **people- and place-based advantages** in their lives. So, we are left with this challenge: how do we make sure that every kid, regardless of class or geography, has ample people- and place-based investments that allow them to develop to their fullest potential?

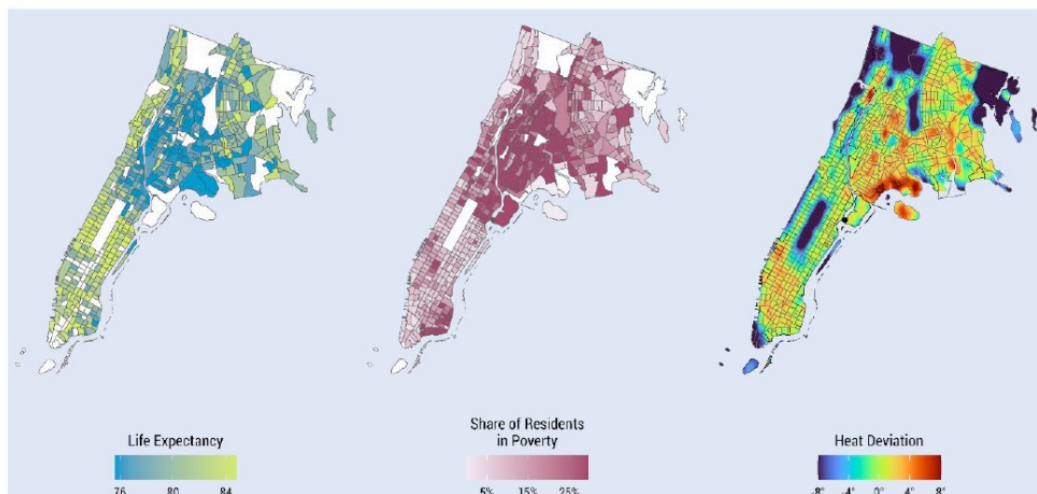
¹ John C. Williams, President and Chief Executive Officer, “X Marks the Spot: Making Missing Markets,” November 14, 2024. Remarks at Intermediating Impact: Making Missing Markets, Federal Reserve Bank of New York, New York City. Available at: <https://www.newyorkfed.org/newsevents/speeches/2024/wil241114>.

This may sound like some sort of utopian experiment, but most of us grew up in that environment **and** it is good business. The reality is that it is expensive to **not** to make these investments. Society bears the costs of not making these investments every day: reduced labor productivity, lower wages, fewer taxes collected, and more strain on multiple systems that handle bad outcomes – treating poor physical and mental health, a bloated criminal justice system, and expensive educational boosts like special education for otherwise healthy children arriving at school not ready to learn. The key insight is that the money is being spent either way. The goal here is to move that spending **upstream** to avoid the **downstream** costs (and suffering). This approach is both more fair and less expensive.

Overlapping Vulnerabilities Have a Silver Lining: Overlapping Resources

The second key insight is that social and economic vulnerabilities overlap. And so do the resources targeting them. The heat maps of Manhattan and the Bronx below show community-level risk through three different lenses: health, economic opportunity, and environmental risk. As you can see, the patterns are very similar. The places with one risk are often at risk for all. This is not unique to New York City; it is a pattern you would see in any community across the U.S.

Figure 1 The Geography of Climate, Health, and Economic Vulnerability



Source: City Health Dashboard, 2021 5-year American Community Survey, New York City. Analysis by Jacob Scott.

The Making Missing Markets initiative wants to build on this recognition of overlapping vulnerabilities by calling for overlapping interventions using new cross-sector/place-based interventions that take advantage of overlapping resources. These new business models should focus on investing upstream in neighborhoods to create new value by avoiding downstream costs. The revenue—or expense savings—attributable to those interventions can be difficult to capture and measure, so this work will require innovations in finance to make them easier to initiate and sustain over the long run. That is the goal of identifying and creating new markets where they don't exist now.

How Does Making Missing Markets Work?

To create a market that results in more opportunity-rich communities you need three simple components: buyers, producers, and connectors.

Buyers. There are multiple entities and sectors that are eager to pay for better economic, health, and resilience outcomes. We conservatively estimate that we spend around \$2.4 trillion every year to address the downstream effects of poverty, poor health, lack of economic opportunity, and vulnerability associated with extreme weather and other harms in the environment. Banks, motivated by the Community Reinvestment Act of 1977 invest over \$400 billion annually into low-income communities. We spent almost half a trillion dollars a year on anti-poverty programs. We are coming close to spending \$1 trillion annually on Medicaid—medical care for the poor—and we know that much of the remaining \$4 trillion in Medicare and private medical spending goes to treat preventable chronic disease and avoidable mental health issues. There are other outlays we could list here, but the bottom line is that the Making Missing Market initiative is an effort to spend those resources upstream to avoid the expensive downstream consequences of not attacking the roots of these problems.

Producers. A producer of health, opportunity, and well-being is any entity or individual who helps a person navigate life's twists and turns and develop themselves to the fullest extent possible. These include all the people-based interventions we need: teachers, nurses, coaches, tutors, scout leaders, etc. And all the place-based interventions: affordable homes, living-wage jobs, good schools, clinics that adopt the whole neighborhood as the patient, grocery stores in food deserts, libraries, etc.

Connectors. Connecting those trillions in downstream spending to the upstream interventions that need that support is not easy. It requires marketcraft, to borrow a phrase from the author Chris Hughes. That includes layered funds that allow multiple investors with varying risk/return profiles to invest, Community Development Financial Institutions, for-profit banks, private equity firms, impact investors, entrepreneurs, creative government financing, and others.

We recognize that this market cannot materialize overnight. And that many of the current resources heading to downstream issues (e.g., treating avoidable chronic disease, getting delayed kids back up to speed in school) cannot be simply stopped. The transition to an upstream-oriented social welfare economy from a downstream-oriented one will require creativity in how we finance that transition in the least disruptive way possible.

The Federal Reserve Bank of NY's Making Missing Markets Initiative—Nuts and Bolts

We are working with hundreds of volunteers that have organized themselves into work groups that are tackling this effort from multiple angles. One is focused on how we incorporate the insights of complex adaptive systems that give us a new framework to analyze problems and propose solutions. Another group is working on new approaches to rural development. Another on connecting all communities to high-speed internet service. One working group is identifying local artists as “guides on the ground” for helping communities develop a vision for improving their communities, which makes them more attractive to investors. And there are many more you can check out on our website.

Good new ideas are great, but to come alive, they need money. That is why we are focused on how to make these ideas sustainable as money-making—or money-saving—endeavors. Creating value in a community is a way to develop revenue or avoid downstream costs. Both approaches can create a reliable cash flow. And a reliable cash flow allows the financial engineers on Wall Street to create new financial models to pay for the needed upstream investments that create that value in

the first place. Several work groups are playing the role of connectors to make it easier to invest in new ideas and new approaches.

Conclusion

To learn if these new approaches can work, we need to try them out in a handful of places to pilot and workshop them. And we need many new partners that can help us develop, execute, and fund these innovative cross-sector/place-based interventions. In the end, we must show the American people that we can use the substantial resources at our disposal to create meaningful opportunities in a way that ensures the economy works for everyone. Please join in the conversation.