



# SBIC Program

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Fostering Investment in  
Underserved Markets

June 17<sup>th</sup>, 2005



# What is the SBIC Program?





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In 1958, Congress passed the Small Business Investment Company Act creating the SBIC Program

- Multi billion \$, government-sponsored “fund of funds”
- Invests long term capital in privately owned and managed investment firms (licensees)
- Public-private partnership
- Administered by the Investment Division, US Small Business Administration

to bridge the gap between entrepreneurs’ need for capital and traditional financing sources.



# What is the SBIC Program?

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- A large institutional LP, managing \$11.8 billion in outstanding leverage and commitments
- An investor in over 400 private equity partnerships
- Supported by diverse private partners providing roughly \$12.5 billion in capital resources to small businesses nationwide

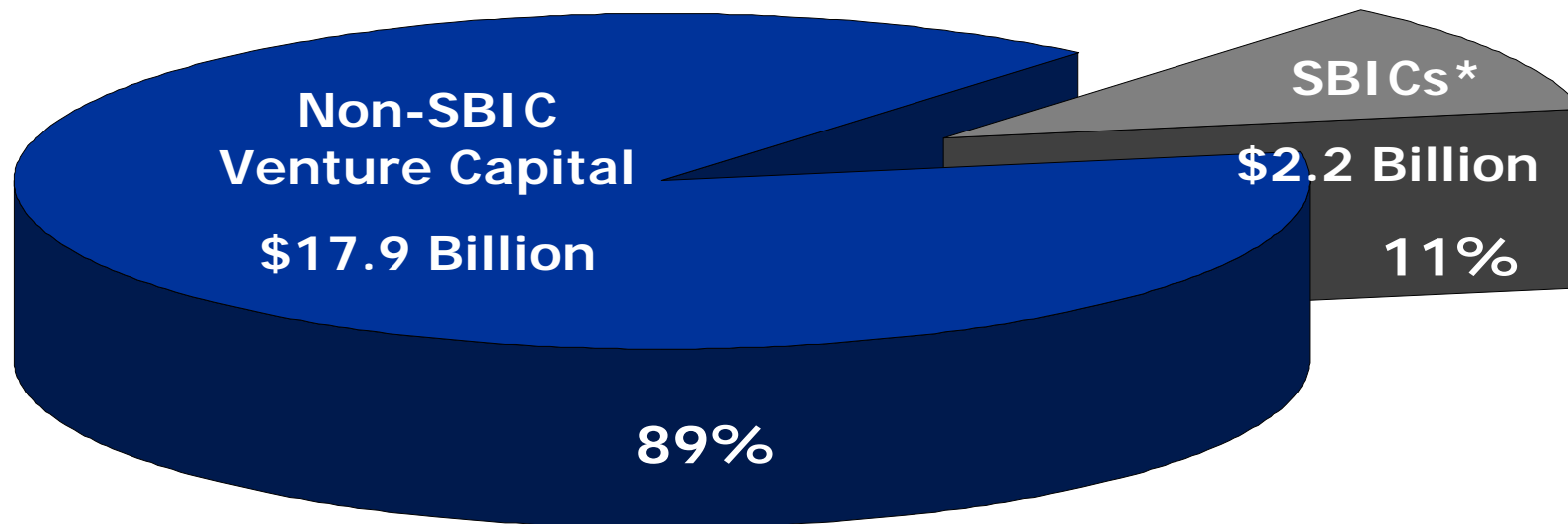
Source: SBIC Data Management Branch, Weekly Report as of 5/25/05



# What is the SBIC Program?

A Vital Part of the US Venture Capital Industry

**In Fiscal Year 2004, SBICs provided 11.2% of all venture financing dollars**



Source: PricewaterhouseCoopers/Thomson Venture Economics/National Venture Capital Association MoneyTree™ Survey. "Venture Capital Finishes at a Solid \$18 Billion for 2003" released 1/27/2004 & "Venture Capital Declined in Q3 2004 with \$4.3 Billion Invested" released 10/26/2004.

\* SBIC Financings include only equity and debt with equity features. Pure debt financings are excluded.



# What is the SBIC Program?

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An Engine for Growth in the US Economy

## **In Fiscal Year 2004:**

- SBIC financings totaled \$2.8 billion
- 2,409 companies benefited from SBIC financing
- \$789 million, or 28% of SBIC financing dollars were invested in companies less than 2 years old
- \$212 million of SBIC financings were made to women and minority owned businesses, a 12% increase from FY2003
- Companies financed by SBICs during FY2004 created 78,800 new jobs



# What is the SBIC Program?

A source of funding for many successful companies

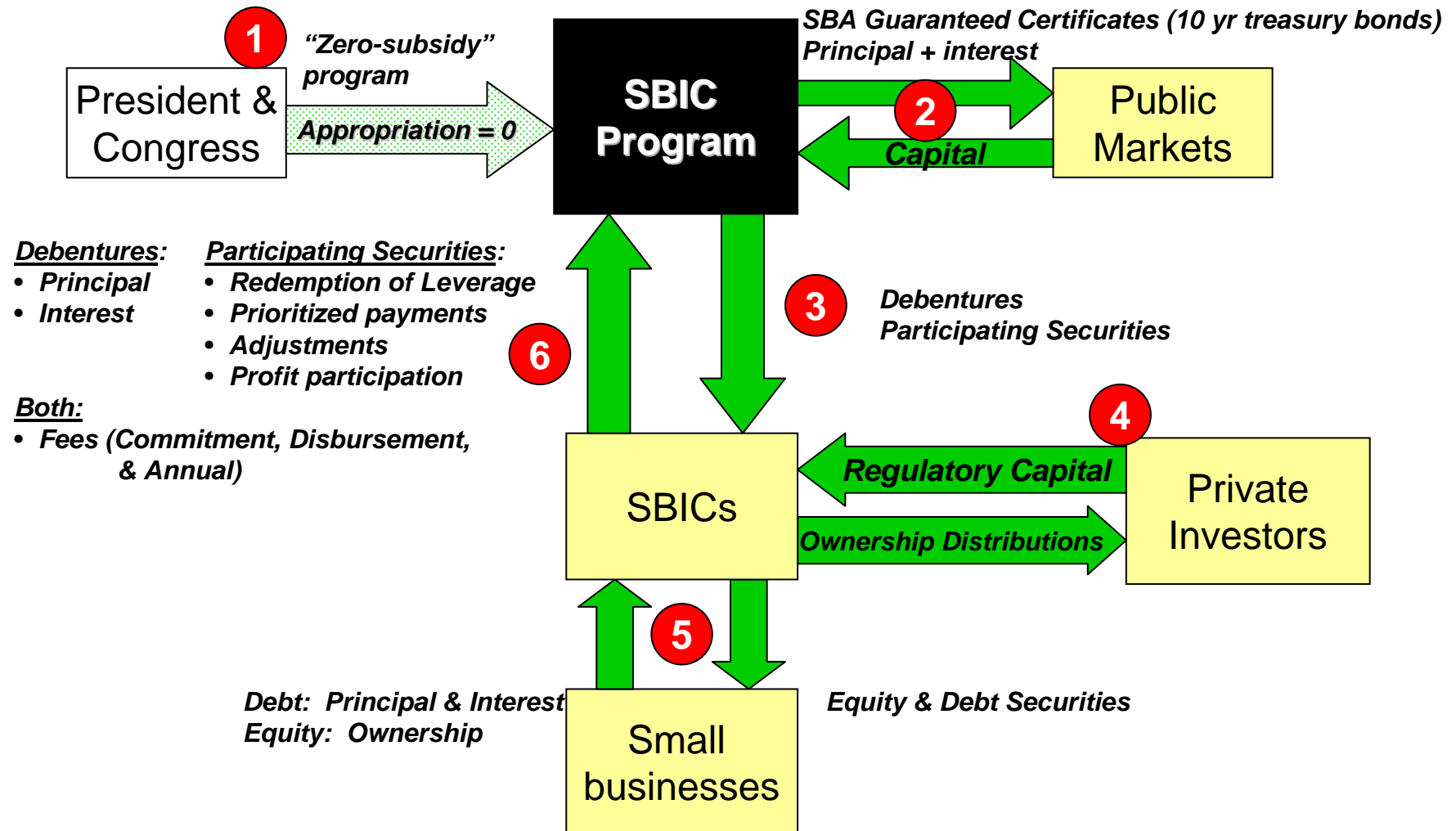
- |                                 |                               |                                |                                |
|---------------------------------|-------------------------------|--------------------------------|--------------------------------|
| A&W Brands Holding Co           | Domain Furniture, Inc.        | Kent Electronics               | Read-Rite                      |
| Actel Corporation               | DoubleClick.com               | Kentucky Kingdom, Inc.         | Restoration Hardware, Inc.     |
| Adaptec                         | Douglas Machine, Inc.         | Kronos, Inc.                   | Rock Bottom Restaurants        |
| Airport Systems Int'l, Inc.     | Duracraft Corporation         | Labor Ready, Inc.              | Sage Software                  |
| America OnLine                  | Etak, Inc.                    | Lam Research                   | Seasafe, Inc                   |
| Amgen, Inc.                     | Educational Development       | LaMadeleine, Inc.              | Security Dynamics Technology   |
| Apple Computer                  | Encore Wire Corp.             | Lifeline Systems, Inc.         | Staples                        |
| Assembly Solutions, Inc.        | Envoy Corporation             | Maxim Integrated Products      | Steelweld Equip. Co.           |
| BeutiControl Cosmetics, Inc.    | Evergreen Solar, inc.         | Metrolina Outreach Mammography | Sun Microsystems               |
| Bright Start, Inc.              | Federal Express               | Microcom                       | Symbol Technologies, inc.      |
| CTC Distribution Services       | Flserv                        | Micromodule Systems            | Synoptics Communications, Inc. |
| Callaway Golf Company           | Fusion Systems Corp.          | Microtouch Systems, Inc.       | Techne Corp.                   |
| Cardio Logic Systems, Inc       | Gendex                        | Mother's Work, Inc.            | Telesis Corp.                  |
| Cerner Corporation              | General Sciences Corp.        | Neoterik Health Tech, Inc.     | Teradata Corp.                 |
| Chesapeake Biological Labs      | Genicom Corp.                 | NetFrame Systems, Inc.         | The Computer Group (TCG)       |
| Citation Computer Systems, Inc. | Geotek Communications, Inc.   | Newcomb Communications, Inc.   | The Last Best Place Catalog    |
| Cognex Corporation              | Global Village Communications | New England Critical Care      | The Merchandising Group (TMG)  |
| Compaq, Inc.                    | Gymboree Corporation          | NuCo2, Inc.                    | The Systems Center             |
| Comptek Research, Inc.          | Hanger Orthopedic Group, Inc. | Octel Communications Corp.     | Tricord Systems, Inc.          |
| Connecticut Culinary Institute  | Harman International Ind.     | Optical Data Systems           | Vertex Communications          |
| Cooper Natural Resources, Inc.  | HS Resources, Inc.            | Orbital Sciences Corp.         | Vivid Technologies, Inc.       |
| Costco                          | Healthcare Compare Corp.      | Outback Steakhouse             | WebMethods                     |
| Cray Research                   | Healthcare Services           | Peoplesoft, Inc.               | Wellfleet Communications       |
| Cutter & Buck                   | HealthSouth Rehabilitation    | Performance Polymers           | Wire Networks, Inc.            |
| Data Stream Systems             | Industrial Training Corp.     | Petstuff, Inc.                 | Extreme Networks, Inc.         |
| Devon Group, Inc.               | Information Analysis, Inc.    | Potomac Group, inc. (MediFAX)  | Zydacron, Inc.                 |
| Digimark, Inc                   | Infotec Commercial Systems    | Protocol Systems               |                                |
|                                 | Intel Corp.                   | RF Power Products              |                                |
|                                 | Jenny Craig, Inc.             | Radio One                      |                                |



How does the program work?



# How does the program work?





# How does the program work?

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## What can SBICs invest in?

- Loans, debt with equity features or equity
- 100% "Small Business"
  - Net worth < \$18M and average after-tax income for prior two years < \$6M
- Of which, 20% must be "Smaller Enterprise"
  - Net worth < \$6M and average after-tax income for prior two years < \$2M
- Not more than 20% of the private, committed capital can be invested in a single company without prior SBA approval
- Project financing is prohibited (real estate, single purpose projects)
- SBICs may control small businesses for up to seven years which may be extended with SBA approval



# How does the program work?

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Customized structures fit managers' & LPs' needs

**Existing or  
Emerging Fund**

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**Standard  
Structure**

**Drop-down  
Fund**

**Side-by-  
side Fund**

**Side-by-side  
with drop-down  
feature**

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**Participating  
Securities**

**Debenture  
Securities**

**CLOSED for FY 2005**



# How does the program work?

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## Debenture Securities

- Best suited for mezzanine / later stage investors focused primarily on debt and debt with equity features
- Interest only, bullet with 10 year maturity
- Interest payments are semi-annual, priced at a spread over 10 Year Treasuries.
- Unsecured, non-recourse to General Partners
- Leverage available up to 3x private capital paid-in, although generally capped at 2x
- Leverage ceiling is \$119 million
- Diminishing prepayment penalty in first five years (5.4.3.2.1%)
- 3% origination / commitment fee plus .855% annual fee on leverage drawn\*

*\* The annual fee is a contingent payment, fixed at time of leverage commitment. The current rate floats according to the SBIC Program's required subsidy rate.*

# How does the program work?

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## Experienced Managers

### **SBICs must meet rigorous requirements to be funded:**

- Senior-level decision making experience in a private equity fund relevant to proposed fund
- Evidence of strong deal flow in investment area for proposed fund
- Investment experience as a principal rather than an agent (i.e. investment banker, consultant, broker)
- Realized track record of superior returns benchmarked against funds of same vintage year and style
- Hands-on experience adding value at the portfolio company level
- Cohesive team, with complementary skills, history and strong chemistry
- Private capital comprised of diverse private LPs



# Underserved Markets



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***Today, “Underserved Markets” exist for early and expansion stage companies that:***

- **Require initial funding less than \$5M**
- **Focus in industries other than IT, life sciences or financial services**
- **Locate outside of Silicon Valley, Boston & New York City**



# Smaller capital requirements

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***The US venture market has moved toward “Mega-funds” that can’t allocate resources to pursue smaller transactions***

Average size of equity financing round	
US Venture Capital – 2002	SBIC Program – 2002
<b>\$7.0 million</b>	\$0.62 million

Source: Venture Economics Avg Round of Financing by VCs in 2002 & SBIC Data Management Branch, Avg Size of Investment, Participating Securities FY End 2002.



# Smaller capital requirements

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***SBA is one of the few large institutional investors that is capable of being a large LP in a small fund.***

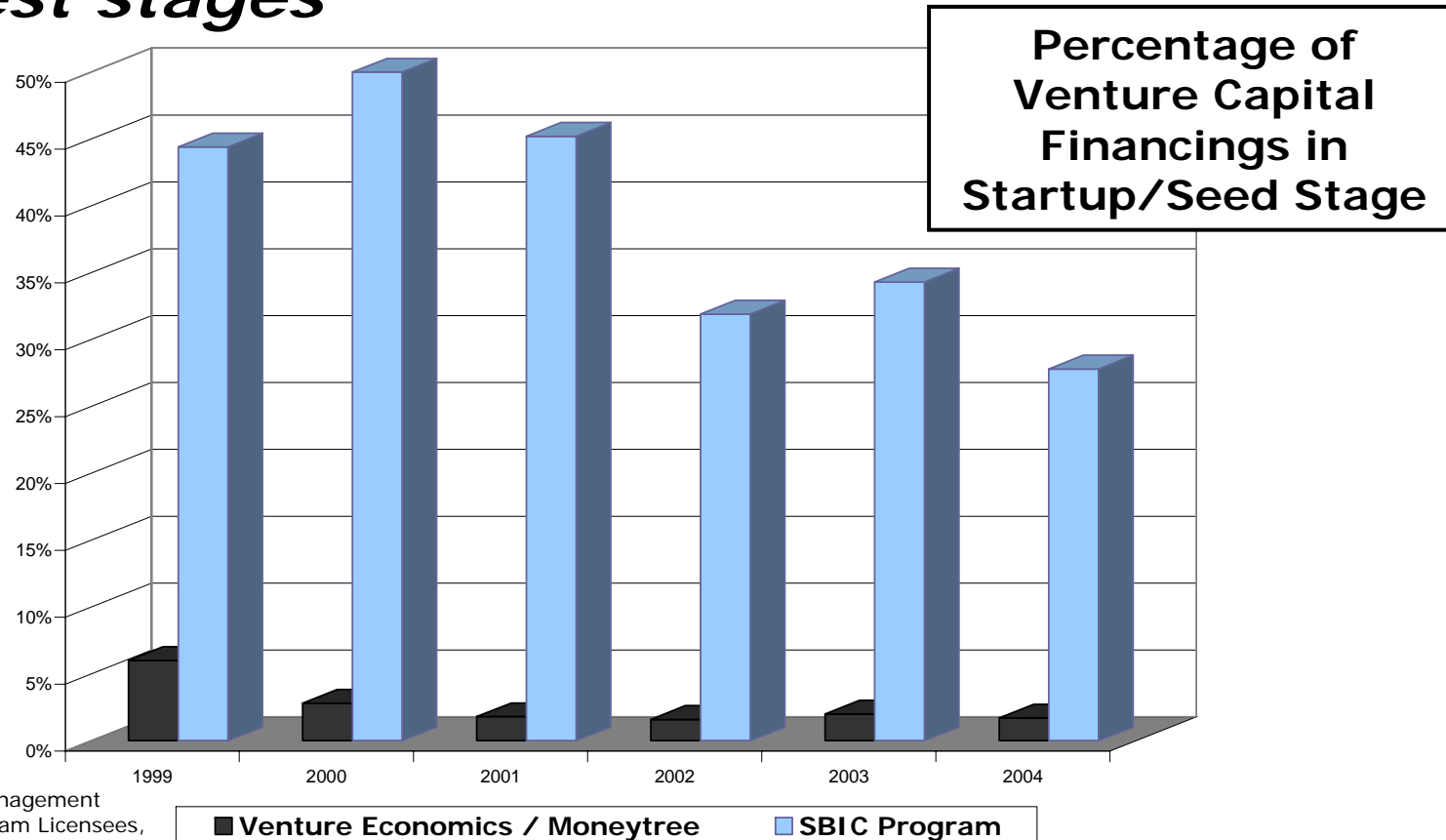
**Smaller funds can pursue smaller transactions which:**

- Are less competitive than larger deals
- Often occur in niche/specialized markets
- Allow equity sponsors to add most value to portfolio companies
- Are less reliant on public market sentiment



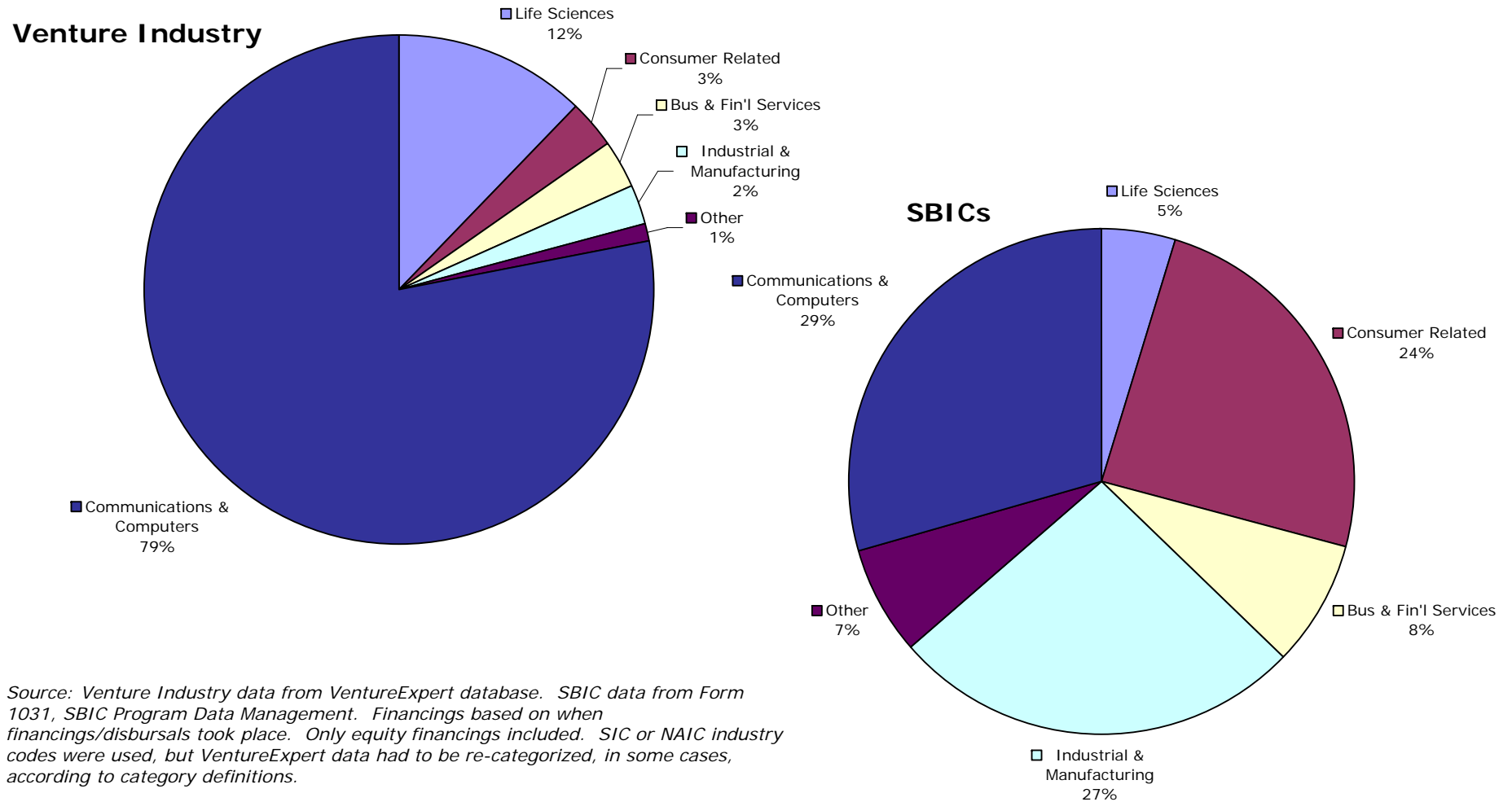
# Smaller capital requirements

***SBICs continue to provide capital at the earliest stages***



Source: SBIC Data Management Branch, All SBIC Program Licensees, % of Financing to Start-up business (aged 2 years or less) & Venture Economics/PWC Moneytree survey

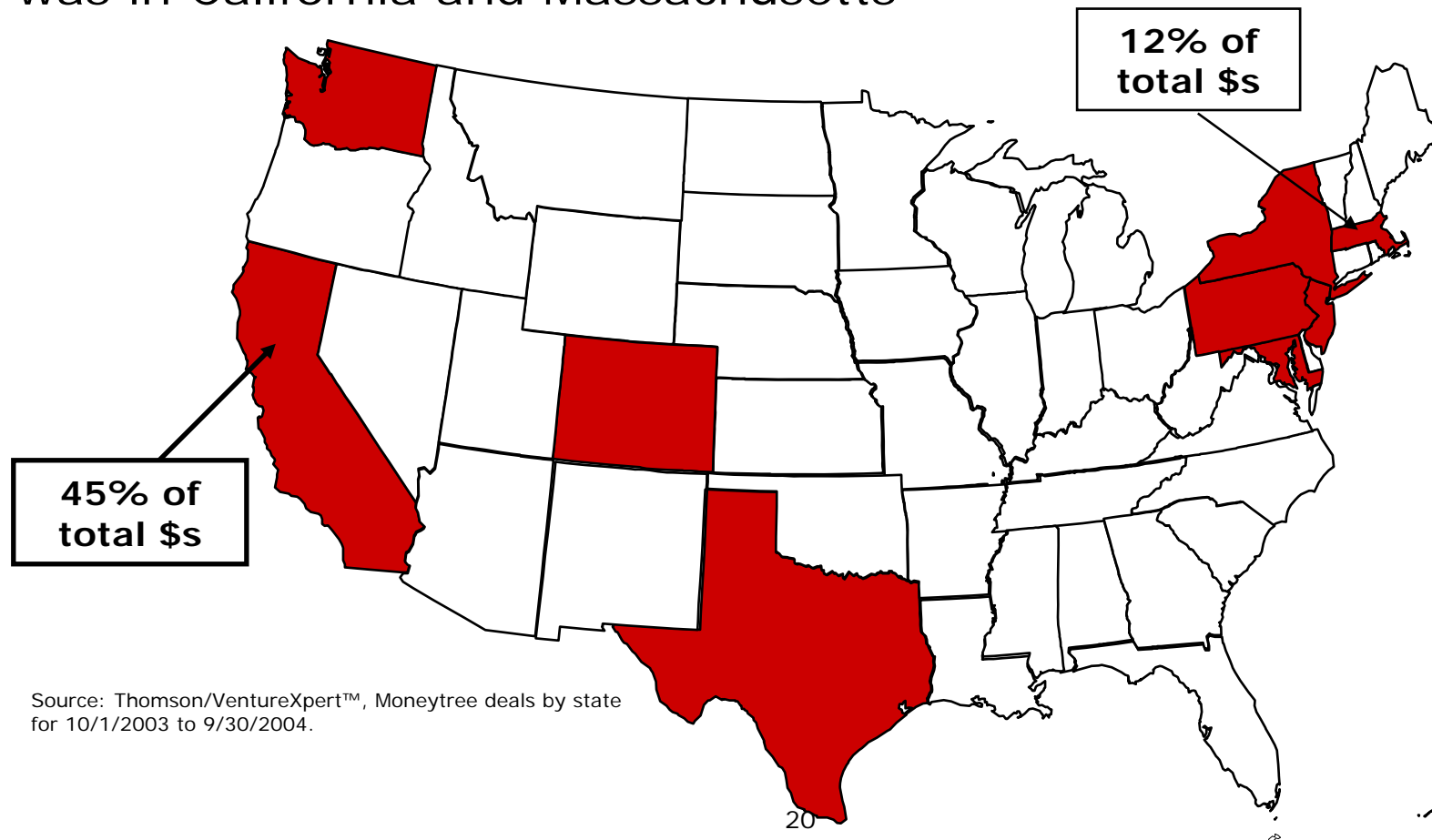
# Underserved industries



Source: Venture Industry data from VentureExpert database. SBIC data from Form 1031, SBIC Program Data Management. Financings based on when financings/disbursals took place. Only equity financings included. SIC or NAIC industry codes were used, but VentureExpert data had to be re-categorized, in some cases, according to category definitions.

# Underserved regions

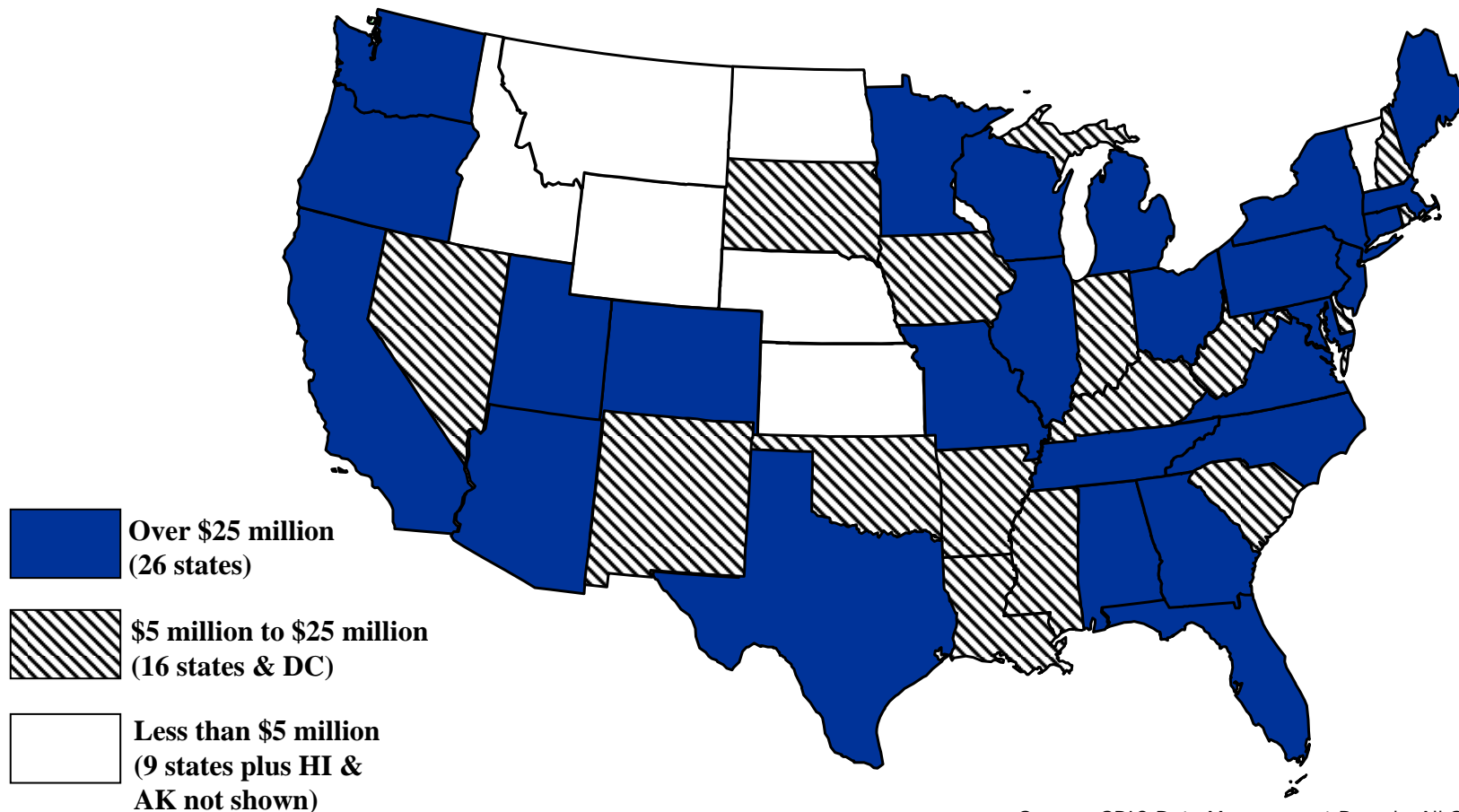
According to Thomson/VentureXpert™, in FY 2004, 85% of venture capital was concentrated in 10 US states, of which 68% was in California and Massachusetts



Source: Thomson/VentureXpert™, Moneytree deals by state for 10/1/2003 to 9/30/2004.

# Underserved regions

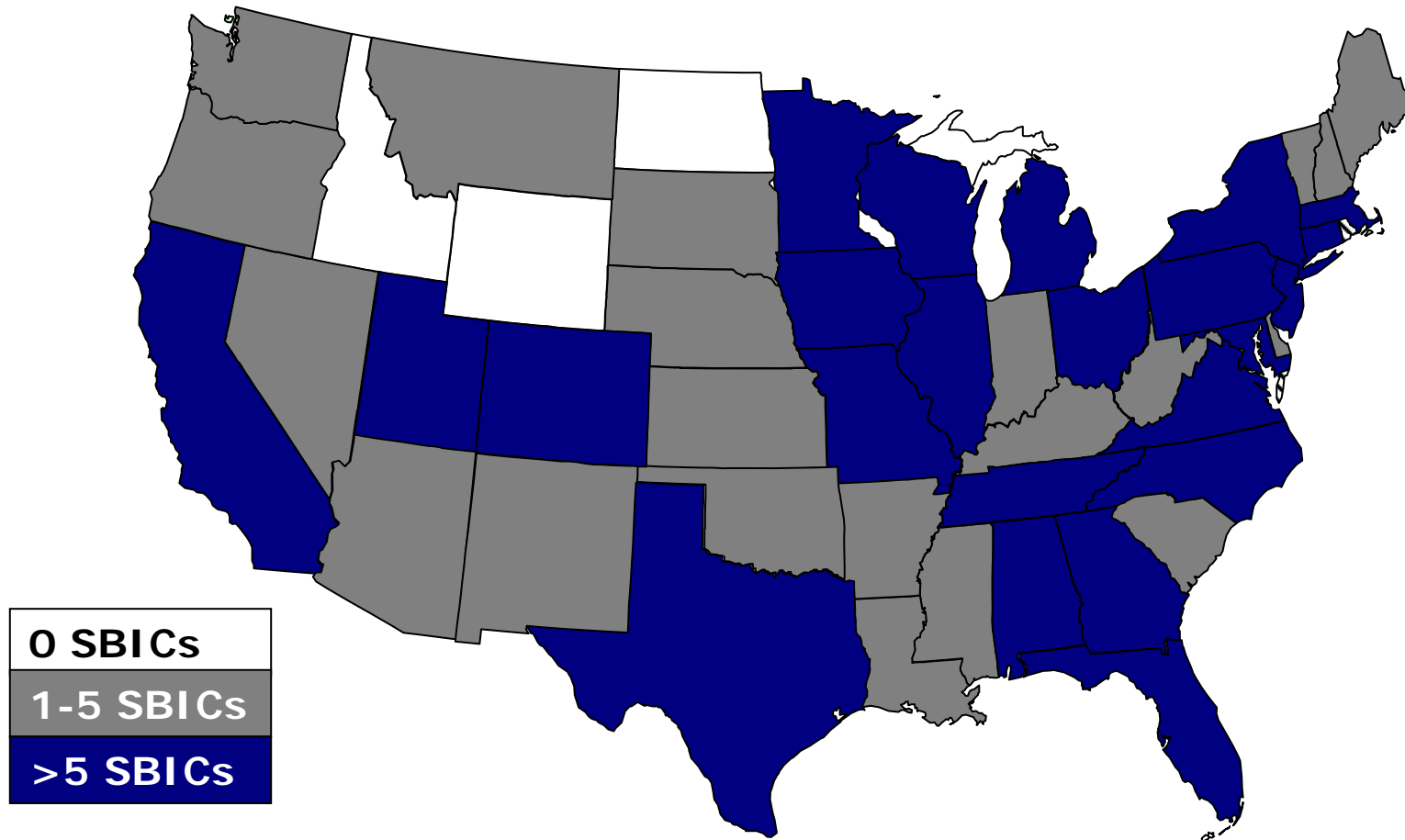
SBIC financing dollars distribution by state for FY2004



Source: SBIC Data Management Branch, All SBIC Program Licensees, Financing to Small Business by State, Reported for FY 2004 as of 06/2005. Total Financing = \$2.837 billion

# Underserved regions

Geographic Distribution of SBICs as of today



Source: SBIC Data Management Branch, SBIC Licensees by state 2004.



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# US Small Business Administration SBIC Program

<http://www.sba.gov/INV>

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