U.S. Small Business Administration

Investment Division

Small Business Investment Company Program

Fiscal Year 2002 Special Report

June 15, 2002

Prepared by
Investment Division
U.S. Small Business Administration
409 Third Street, S.W.
Washington, D.C. 20416

45 Years:

Encouraging innovation, entrepreneurship and economic growth through investment in privately managed funds.

General Disclaimer

This Special Report on the Small Business Investment Company ("SBIC") program contains the first set of "financial statements" produced by the SBA Investment Division. Neither the report nor the financials contained herein have been audited; however, SBA's Office of Inspector General and the General Accounting Office have periodically inspected both the underlying SBIC data and processes used to create this report.

Numerous figures and charts appear throughout this document. All data has been individually footnoted to describe the source, assumptions, limitations, and other pertinent disclaimers. This has been done to minimize problems in extracting charts and figures from this document, and to avoid information being misinterpreted. A few general points are noted below:

- Data Sources: Numerical figures and information are derived or retrieved from tables and reports provided by Data Management in the Investment Division, public studies and websites, government websites, Venture Economics, VentureExpert, PriceWaterhouseCoopers (PWC), and other sources of information, as footnoted and referenced within the document.

- Data Management: Data tables and reports provided by Data Management used in this analysis include data maintained by Investment Division personnel, as well as data provided by SBICs in SBA Form 468s (Statement of Financial Position) and Form 1031s (Portfolio Financing Report) for reported financings.

- Financing Data: SBIC financing data (retrieved from 1031s), when benchmarked against venture capital, is based on the fiscal year when the financing/disbursement of funds took place. Similar to the rest of the industry, financing data may suffer reporting lags. Annual financing data by the fiscal year in which it was financed is subject to change as new reports are filed. For this reason, the SBIC Program Statistical Package tracks when financings are reported, rather than when financings actually occur. The term "Reported Financings" indicates financing data reported that year. However, in order to compare data against industry benchmarks, we have used the date disbursements actually occurred. This report uses PWC MoneyTree data to compare SBIC financings to venture capital. While it is known that many SBICs are included in the PWC MoneyTree survey, all SBIC financings may not yet be included. In addition, economic data from Form 1031 is not audited.

- Economic Information: Much of the SBIC economic information (e.g., revenues, jobs, and taxes) are retrieved from the schedule database based on Annual Form 468. Although SBICs are required to complete this form annually, it is unaudited. Moreover, not all SBICs submit the report. Since multiple records exist for each company, only the last (most recent) record was used to identify the economic data to avoid double-counting of figures. Companies are identified by their employer ID number, when available. When unavailable, employer name was used to identify the company. Analyses disregard percentage of ownership by the SBIC. In addition, SBIC Licensees may have used data from previous years to provide estimated figures. Data entered prior to 2000 was removed from the data set (approximately two-thirds of the data). Of those licensees reporting in 2000 or later, approximately 10% did not provide employee data, about 14% did not provide revenues, and about 84% did not include federal taxes. Because only reported numbers were used (i.e., no figures were either estimated or extrapolated), these figures may be low. All statistical equations were calculated using Microsoft Excel tools.

- Industry Codes: The SBA utilizes North American Industry Classification System (NAIC) codes. These codes were recently updated in FY 2002. Past SBIC information has been categorized in Standard Industrial Codes (SIC) and/or previous (to FY 2002) NAIC codes. Using a table identified in the U.S. Census site, all codes were converted to NAIC FY 2002 codes and then individually mapped by NAIC code against PWC and VentureExpert industries to provide benchmarking. Since there is no explicit mapping of NAIC codes to PWC and VentureExpert industries, an Investment Division analyst developed this mapping based on definitions.

- Financials: The SBIC financial statements were prepared from the program office data for commercial presentation purposes and may differ from the figures presented in SBA's audited financial statements.

Small Business Investment Company Program
Fiscal Year 2002 Special Report

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1. Letter from the Associate Administrator for Investment

Dear Reader,

Welcome to this "Special Report" on the State of the Small Business Investment Company ("SBIC") program. After forty-five years of being in business to support America's entrepreneurs, we thought it was time you knew more about the SBIC program and where it is headed.

SBICs – privately-owned and managed venture capital funds – are the building blocks of long-term economic prosperity. At the end of FY 2002, SBIC investments supported over 10,800 entrepreneurial companies in 441 funds, with over $11.8 billion in private venture capital and another $5.1 billion in SBA matching funds.[1] As this report shows, SBIC financings work to fill the gap in private equity markets, especially at the earliest stages of a company's growth.

The program is a unique way for the federal government to help U.S. small businesses. It is structured so that the government itself does not make direct investments or target specific industries. Essentially a "fund of funds," the SBIC program outsources the portfolio management and investment decisions to qualified private fund managers, who invest in entrepreneurial companies based on their specialized knowledge of venture capital investing.

Alongside private equity, the government acts as a limited partner, seeking a return on its investment. In the broadest sense, those returns are in the form of major contributions to U.S. economic productivity, employment, and innovation:

> ***SBICs – both leveraged and non-leveraged funds – are part of a legacy of early investing in some of the world's most successful companies – America Online, Apple Computer, Callaway Golf, Costco, Federal Express, Intel, Outback Steakhouse, PeopleSoft, Staples, and others.***

Of course, even with the program's success stories, there is no way to sugarcoat the fact that anyone who has invested in venture capital has felt the pain associated with the decline in private equity markets over the last three years. SBICs are not immune to that decline. The SBIC program is a "zero-subsidy" program, supported by fees paid by the SBICs. As such, the program must be able to operate in a manner that ensures the return of SBA's capital – and provides the federal government with a fair share in the profits of successful funds – to keep the program self-financing over the long term.

We view the current market environment as an opportunity for SBICs to prove their worth like never before. At a time when private investors are questioning their commitment to the venture capital asset class, SBA leverage – government-guaranteed matching investment funds – attracted $800 million in private capital in FY 2002 alone. By encouraging private risk-taking, the program is capable of supporting thousands of entrepreneurs through the slow economic period, with the prospect of growing leading-edge businesses out of the down cycle.

[1] Figures obtained from SBIC Data Management.

Business Activities of the Investment Division

The Investment Division is running more like the business it is. We are executing an ambitious plan that puts into action several elements of the President's Management Agenda, the Administration's Agenda for Small Business, and the SBA's Strategic Plan. We are meeting or exceeding our performance objectives with respect to SBIC licensing, financings, examinations, and restructurings. With guiding principles, performance goals, and program priorities firmly in place, the Investment Division is continually reassessing its business plan to ensure that it produces measurable results.

Special Report. This Special Report is part of our new orientation – a starting point for reviewing SBIC portfolio performance while managing risk, fostering accountability, and demonstrating program results. In this report, we seek to describe the potential risks and rewards of taxpayers' participation in the SBIC program.

> ***As this report shows, SBICs have helped generate billions of dollars in corporate revenues and income taxes, while creating over one million jobs and countless improvements to our health, safety, and way of life. These benefits continue to pay America many times over for the costs of running the program.***

SBIC Licenses. The licensing process for new SBICs is the most critical element of our risk management strategy. Important measures are being implemented to increase the percentage of profitable funds in the future and to protect against the risk of financial loss to SBA and private investors. We are striving for a high degree of customer service, a rigorous approach to due diligence, a high level of coordination and teamwork, and strong consistency in our decision-making. We are excited about the teams of venture fund managers we are licensing today from across America.

Of course, the day we license a fund is the day we assume the risk that some or even all of SBA's investment may not be recovered. That is why we are focused on licensing qualified funds *and* rejecting applications that do not meet our licensing criteria. We respect the specialized nature of venture investing. SBIC application denials or dismissals are critical contributions to program risk management.

Annual SBIC Examinations. In FY 2002, the Office of SBIC Examinations performed a record 326 annual examinations. At the same time, the number of reports with compliance issues has declined from seventy-six in FY 2001 to seventy-one in FY 2002. We remain vigilant in our efforts to guard against fraud and other wrongdoing in the SBIC portfolio. We are seeing fewer improper financings, inappropriate distributions, conflicts of interest, and portfolio valuations that did not follow our guidelines.

In line with the President's Management Agenda for federal agencies, we have competitively outsourced a portion of these exams, starting with the non-leveraged SBICs that present no financial risk to the government.

Portfolio Oversight and Risk Assessment. The Office of SBIC Operations is undergoing change to dedicate more internal resources to risk management, better define portfolio company value, and establish clear policies and procedures for managing our portfolio. We believe we have an opportunity to play a prominent role in encouraging best practices in venture capital fund management, which is important not only to the integrity of the program but to the industry overall.

With the assistance of private fund managers, the Investment Division has built a new portfolio risk rating model to replace the current system of monitoring SBICs for regulatory and financial warning signs. When this tool is fully integrated into day-to-day oversight later in FY 2003, the program will benefit by having a more standardized system for assessing and managing risk at various stages of an SBIC's life. Over time it will also provide us with more information regarding total prospective portfolio losses, including where they fall in the range of SBIC program assumptions.

Underserved Markets

The days when venture capital consisted of financing companies only in Boston, or New York, or Silicon Valley, are long since over. Great companies can be found in every corner of this country. SBICs recognize that opportunity.

The economic impact of SBIC financings is felt in all 50 states, plus the District of Columbia, Puerto Rico and the Virgin Islands. In FY 2002 alone, over 1000 SBIC investments – with a value of over $725 million – were reported in low and moderate income (LMI) areas.[2]

We are encouraging geographic diversity and investment in underserved markets through the use of available financial tools and aggressive outreach efforts. Fund management teams are using LMI Debentures (low-interest debt with no interest payment due for the first five years) to invest in LMI areas. SBICs, both leveraged and non-leveraged, remain excellent vehicles for investors to receive Community Reinvestment Act (CRA) credit for their investments.

Our long-term vision is to expand the reach of venture capital into every nook and cranny of America. American communities that are currently overlooked or underserved by venture capital can offer huge rewards to investors. We are dedicated to licensing qualified fund managers who seek to take advantage of those opportunities – managers who, with their venture investing experience and networks, can create lasting economic development and employment in urban, rural and struggling communities throughout America.

We hope this Special Report provides a better picture of what one of SBA's premier programs has contributed to the spirit and success of U.S. entrepreneurship. SBICs are unique public-private partnerships that, through the highs and lows of the market, help fuel the engines of growth in our economy – America's small businesses.

Sincerely,

Jeffrey D. Pierson
Associate Administrator for Investment

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[2] Figures from Data Management using figures reported in FY 2002, not when financings actually occurred.

Statistical and Financial Highlights

The Financings

- Through 2002:
  - Total Financings from April 1959 through FY 2002:
    - $37.7 billion
    - Over 90,000 different small business concerns financed (estimated)
  - Total SBA Disbursements through FY 2002: $10 billion
    - $9.3 billion in leverage
    - $648.9 million in advanced prioritized payments paid by the SBA.

- Reported in FY 2002:[3]
  - Reported Financings:
    - $2.7 billion; $841.9 million (31.9%) under 2 years in age
    - 1,979 different companies; 730 under 2 years in age
    - 4,004 financings
  - SBA Poolings: $1.1 billion
    - Participating Security: $813.5 million
    - Debenture: $289.1 million

- Venture Benchmarks FY 1994 through 2002:[4]
  - SBIC financings represented 8% of Venture Financings dollars
  - SBIC financings represented 64% of Seed Financings dollars

The Economics

- Jobs in SBIC Portfolio Companies FY 2002 (see Section 3.1 for more information on numbers):
  - ***Created*** (Using National Venture Capital Association ("NVCA") industry ratio)[5]: 73,000 jobs
  - ***Sustained with FY 2002 Financings*** (Number of jobs in companies financed by SBICs in FY 2002, based on unaudited pre-financing economic data - Form 1031s)[3]: 176,309 jobs
  - ***Total Supported*** (Number of jobs held by companies in which SBICs held a financial interest, based on unaudited Annual Report Schedule data - Form 468)[6]: 1.1 million
- Revenues in SBIC Portfolio Companies FY 2002 (based on pre-financing data as reported in Form 1031) [3]: $14.8 billion
- Taxes FY 2002 (based on unaudited Annual Report Schedule Data as reported in Form 468)[6]: $6 billion
- Geographic Reach: From FY 1994-2002, SBICs provided over $26 billion in financings, covering all 50 states, District of Columbia, Puerto Rico, and the Virgin Islands.
- Industry Diverse[7]: Between FY 1994 and 2002, SBICs provided financings across diverse industries, providing 65% of SBIC financing dollars to non-technology and life sciences, as compared to the overall venture industry with only 9% of all venture financing dollars in that category.

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[3] Based on when the Investment Division received 1031s (notification of financings), not when the financings actually occurred.
[4] Venture Capital Financings figures as reported by PriceWaterhouseCoopers (PWC) (www.pwcMoneyTree.com) and VentureExpert. See Exhibit 2 and 8 for further information on notes related to these numbers.
[5] Three Decades of Venture Capital Investment Yields 7.6 Million Jobs and $1.3 Trillion in Revenue - Research Finds That $36K of VC Investment Creates a US Job", NVCA October 22, 2001 Press Release, on NVCA.org website. See section 3.1 in this document for full disclaimer information regarding this number.
[6] This data was retrieved from the schedule database provided by Data Management. The schedule database is based on Form 468 that each SBIC is required to submit to SBA on an annual basis. The data is not audited. See exhibit 13 within this document for further information.
[7] Venture data from VentureExpert database, using MoneyTree data set for FY 1994-2002. SBIC data from 1031s based on financing dates. Industries based on VentureExpert industry definitions. See Exhibit 24 for further notes related to these numbers.

FY 2002 Consolidated SBIC Licensee Portfolio (In Millions of $)

Fund Type	Number of Licensees	Private Regulatory Capital ($M)	SBA Capital ($M)			Combined Committed Resources ($M)
			Outstanding Leverage	Commitments	Total	
Participating Security	185	4,285.8	3,297.3	2,919.5	6,216.8	10,502.6
Debenture	128	1,880.2	1,336.7	725.6	2,062.3	3,942.5
*Bank-owned	87	5,392.1	23.2	10.0	33.2	5,425.3
SSBIC	42	119.3	67.6	12.9	80.5	199.9
TOTAL	442	11,677.4	4,724.8	3,668.0	8,392.8	20,070.3

Based on Annual Reports (Form 468s) for SBIC licensees that were active at the end of FY 2002:

Fund Type	Total Assets ($M)	% of Total Assets	Loans and Investments			SBA Leverage / Private Capital
			At Cost ($M)	At Value ($M)	Value/Cost	
Participating Security	4,356.3	20.3%	3,890.6	3,892.8	1.00	1.28
Debenture	2,742.8	12.8%	2,760.2	2,399.3	1.06	.92
*Bank	14,200.2	66.1%	7,884.7	8,442.0	1.07	.01
SSBIC	197.3	0.9%	134.4	140.8	1.05	.70
TOTAL	21,496.6	100%	14,669.8	14,874.8	1.05	.43

**Note: Bank-owned funds are usually funds with little to no leverage, as indicated. Because they are a significant part of financings and capital base with little financial risk to the government, they are often separated for analysis purposes.*

See Section 5 of this report for further analysis of SBIC licensee portfolio.

Selected SBIC Program Financials

	Cumulative FYs 1994 through 2002 ($M)			Consolidated Program		
	Debenture	Participating Security	Cum. Total	FY 2001 ($M)	FY 2002 ($M)	% Change
P&L						
• **Appropriations**	79.5	149.4	228.9	26.2	0	-100%
• **Other Revenues**	84.9	436.1	521.0	139.2	73.8	-47%
• **Net Income**	75.2	289.1	364.2	135.6	(213.0)	-257%
BALANCE						
• **Total Assets**	1,462.4	3,570.1	5,032.3	4,428.9	5,032.3	13.6%

See Section 4 of this report for further information regarding SBIC Program Financials.

2. Business Description

2.1 Overview

In 1958, Congress passed legislation creating the Small Business Investment Company Program. Back then, almost all innovation, job creation, and economic growth was thought to come from large corporations. The SBIC program literally created the venture capital industry – a new asset class – to bridge the gap between entrepreneurs, looking to start or grow their businesses, and traditional financing. Forty-five years and over $37.7 billion in small business financings later, the program's mission remains the same:

> ***Our mission is to improve and stimulate the national economy in general and the small business segment thereof in particular by establishing a program to stimulate and supplement the flow of private equity capital and long term loan funds which small business concerns need for the sound financing of their business operations and for their growth, expansion, and modernization, and which are not available in adequate supply: Provided, however, That this policy shall be carried out in such manner as to insure the maximum participation of private financing sources.***

We accomplish our mission by:

- licensing top fund managers with exceptional deal flow;
- seeking participation from major private investors;
- managing risk to taxpayers through standardized risk management procedures;
- communicating understandable program ground rules;
- offering funds time to develop results, given the cyclical nature of venture investing; and
- focusing on profit maximization

One of the most common misperceptions about the SBIC program is that it is a *credit* program only. While not a true venture capital program where all limited partners' commitments would be equally at risk (the government has the ability to limit its financial exposure in certain circumstances), it is nonetheless a unique public-private *investment* program. Typical tools and methods for limiting "credit risk" to taxpayers – essentially by monitoring interest payments – are not suitable for the equity portions of the SBIC portfolio.

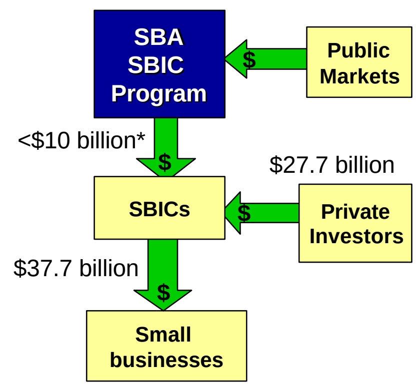
Today there are two types of SBICs - the original SBICs, licensed under Section 301(c) of the Small Business Investment Act ("Act") and Specialized Small Business Investment Companies ("SSBICs"), licensed under Section 301(d) of the Act. SSBICs specifically target entrepreneurs who have been denied the opportunity to own and operate a business because of social or economic disadvantage. The Small Business Program Improvement Act of 1996 repealed Section 301(d) and, as a result, no new SSBIC licenses are being issued. However, existing 301(d) licensees were "grandfathered" and are still in operation. With few exceptions, the same rules and regulations apply to both "regular" SBICs and SSBICs. Therefore in general in this report, the SBIC name is used to refer to both SSBICs and original SBICs simultaneously.

Although the government doesn't invest money directly in small businesses, the SBIC program ensures that funds are available to small businesses by providing comparatively inexpensive capital to professional privately managed venture funds that provide equity capital, long-term loans, and debt-security investments, as illustrated in Exhibit 1.

In addition, as shown in Exhibit 1, the SBIC program harnesses private capital alongside its SBA-guaranteed funds (in the form of either debentures or participating securities), providing a much larger base of capital for investments. While over $37.7 billion in small financings have taken place through this program, less than $10 billion came from SBA-guaranteed funds.[8]

Exhibit 1 – SBIC Program: Investing in Small Businesses Since 1958

1958 Through FY2002



**Note: Includes $649 million in advanced prioritized payments.*

From a venture investment standpoint, both the federal government and private equity investors put money into SBICs with the understanding that under a worst case, that there could be a total loss of their investment. Sophisticated private investors are willing to assume that risk based on their confidence in SBIC management teams to produce acceptable returns. When participating securities are used, the government assumes the risk of total loss of investment based on its sharing in the same prospective returns as private investors – to help the program remain self-financing – but also on the expectation that SBIC investments will contribute significantly to U.S. economic productivity, job growth, and innovation.

Not only does private investor capital provide a larger financing base, but it also ensures that all SBIC fund managers are profit-motivated. As with traditional venture funds, the managers of the funds earn incentive fees that are tied to fund profitability (known as the "carry"). The funds make their money on the success of their investments. Thus, their success is closely aligned with that of the small businesses in which they invest.

For that reason, SBICs, in addition to investing capital, provide hands-on involvement in their portfolio companies, including:

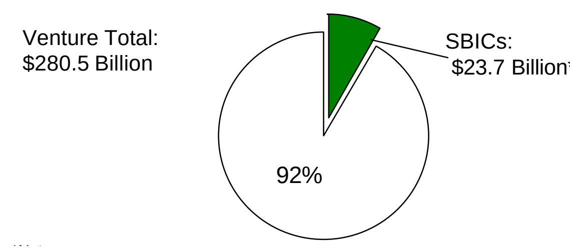
- board participation;
- corporate governance;
- strategic planning and marketing;
- recruitment;
- financial support;
- capital raising; and
- company exit support.

A 2002 study conducted by Stanford University stated: "Evidence strongly points in one direction: venture capitalists provide value-added services, help to professionalize the companies they finance, and help their companies establish themselves in the marketplace."[9] Therefore, small businesses not only receive capital, but critical expertise to grow their company.

[8] Financing data received from Data Management as an update to Table 1 from the Statistical Package and Table 36 – Disbursements from 1959 through September 30, 2002. Disbursements include $9.3 billion in leverage and $648.9 million in advanced prioritized payments.
[9] Hellmann, Thomas and Puri, Manju, On the Fundamental Role of Venture Capital, *Federal Reserve Bank of Atlanta Economic Review*, Fourth Quarter 2002, page 22.

2.2 Venture Capital Industry

Exhibit 2 – FY 1994-2002 Venture Capital Financing[10]



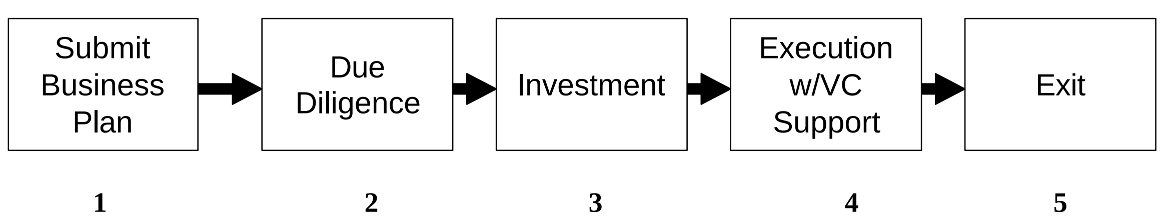
Industry Description. As shown in Exhibit 2, SBICs form a subset of the overall Venture Capital ("VC") industry that provided over $280 billion in financing between fiscal years 1994-2002. VCs address the funding needs of entrepreneurial companies that for reasons of size, assets, and stage of development cannot seek capital from more traditional sources, such as public markets and banks.

Venture capital differs from traditional financing sources in that venture capital typically:

- focuses on young, high-growth companies ;
- invests equity capital, rather than debt;
- takes higher risks in exchange for potential higher returns;
- has a longer investment horizon than traditional financing; and
- actively monitors portfolio companies via board participation, strategic marketing, governance, and capital structure

How Venture Capital Returns are Generated. A business looking for venture capital typically can expect the following process:

Exhibit 3 - Venture Capital Process



1. **Submit Business Plan:** The venture fund reviews an entrepreneur's business plan, and talks to the business if it meets the fund's investment criteria. Most funds concentrate on an industry, geographic area, and/or stage of a company (e.g., Start-up/Seed, Early, Expansion, and Later).

2. **Due Diligence:** If the venture fund is interested in the prospective investment, it performs due diligence on the small business, including looking in great detail at the company's management team, market, products and services, operating history, corporate governance documents, and financial statements. This step can include developing a term sheet describing the terms and conditions under which the fund would make an investment.

[10] Note 1: Total 2002 Venture Capital Financing figure as reported by PriceWaterhouseCoopers (PWC) (www.pwcMoneyTree.com), Full Year and Q4 2002 Results MoneyTree Survey and Historical Trend Data file: National_Aggregate_Data 95Q_02Q4.xls. All SBIC financings may not have been covered within the PWC survey.
Note 2: SBIC figures include only SBIC financings with equity features, based on financing/disbursement date. This figure may be incomplete, as the Investment Division receives reports of financings for a particular fiscal year only after the end of that year.
Note 3: All SBIC financings may not have been covered within the PWC survey from which the total Venture Capital financings figure was derived. The Investment Division expects to work to improve SBIC coverage in these statistics for future reports.

3. **Investment:** If at the completion of due diligence the venture fund remains interested, an investment is made in the company in exchange for some of its equity and/or debt. The terms of an investment are usually based on company performance, which help provide benefits to the small business while minimizing risks for the venture fund.

4. **Execution with VC Support:** Once a venture fund has invested, it becomes actively involved in the company. Venture funds normally do not make their entire investment in a company at once, but in "rounds." As the company meets previously-agreed milestones, further rounds of financing are made available, with adjustments in price as the company executes its plan.

5. **Exit**: While venture funds have longer investment horizons than traditional financing sources, they clearly expect to "exit" the company (on average, 4-6 years after an initial investment) – since that is generally how they make money! Exits are normally performed via mergers, acquisitions, and IPOs. In many cases, venture funds will help the company exit through their business networks and experience.

Venture Fund Investment Cycles. Since it can take 4-6 years for a venture fund to exit a business, investors in the fund must be willing to wait for their returns. This is why venture funds typically experience what is known as the "J" curve (Exhibit 4) in terms of returns to the investor. Returns tend to be negative for a few years at the beginning of a fund's investment cycle because cash is used for investment and management fees, and investments are carried at cost or occasionally written down.[11]

Exhibit 4 – Typical Venture Capital "J" Curve[9]

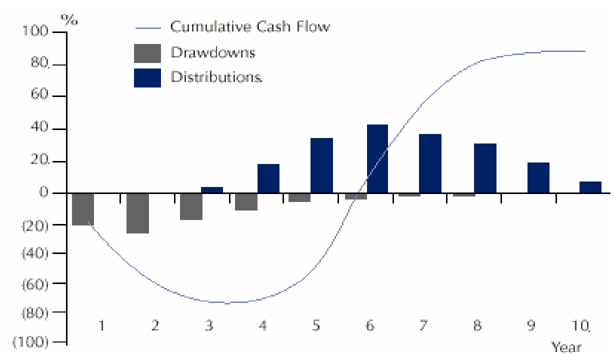
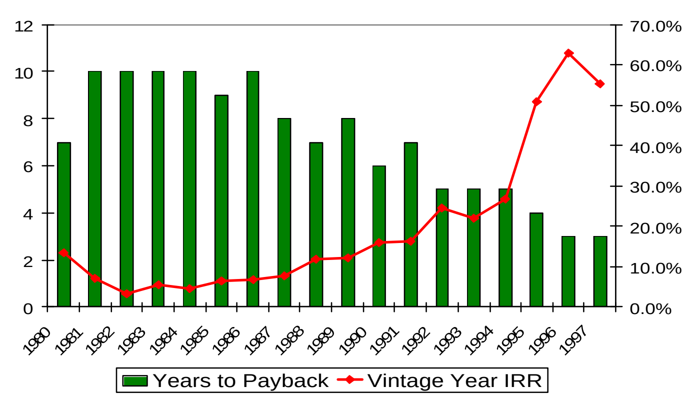


Exhibit 5 shows the average number of years before investors' capital is returned from a venture fund by "vintage year" – the year the fund was formed and started to invest. As shown, it took as long as ten years during the early 1980s, but only three years for vintage year 1997 funds, before investors saw positive returns. One can also see that in general, the shorter the time to payback, the higher the cumulative IRR for the fund. It is difficult to predict how long it will take the more recent venture funds to return capital to investors. For example, as of December 2001, the 1998 funds on average distributed 58% of paid-in capital. Therefore, it is possible that the payback time could stretch anywhere from 5-10 years for funds in the 1998-2001 vintage years.

Exhibit 5 – Average Number of Years before Investors' Capital is Returned from Venture Fund by Vintage Year[12]



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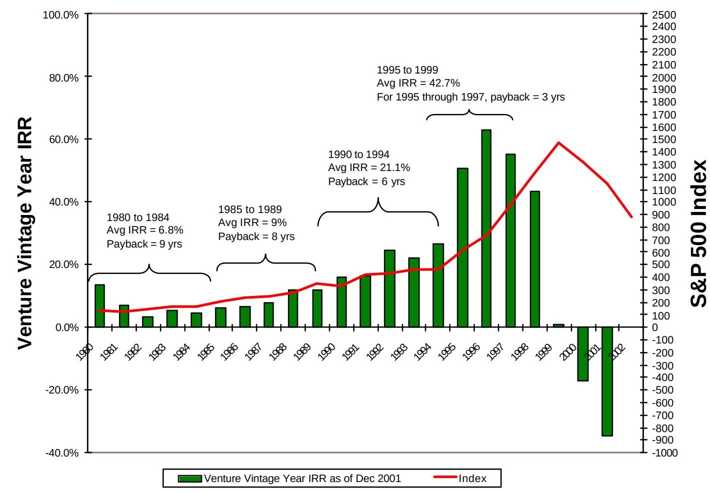
[11] EVCA website: http://www.evca.com/html/investors/inv_why_03.asp

[12] Data derived from Thomson Financial Venture Economics 2002 Investment Benchmarks Report, Page 46, Figure 3.012, Vintage Year Results by Fund Age (in Years) After Formation, Cumulative Average Distribution to Paid-In. Payback years were identified as the year when Cumulative Average Distribution to Paid-In ratio exceeded 1.

Exhibit 6 - Venture Fund Vintage Year Average Cumulative IRRs vs. S&P Index (as of December 2001)[13]



"Time to exit" can depend on the nature of the company in terms of both its operating history and its position in the industry, but the overall economy and stock market usually drive the outcome. The chart to the right (Exhibit 6) shows the average fund cumulative internal rate of return ("IRR") as of December 2001. Vintage year appears as columns on the left axis, alongside the S&P Index as a line on the right axis across the years 1980-2001. In general, the IRRs of venture funds are tied to the rise and fall of the stock market.

An example is vintage year 1996, when the highest average return preceded the high S&P index by three years. In other words, it would appear that the time to invest in venture capital is roughly two to three years prior to a peak in the market – when company valuations are lower – following the classic "buy low – sell high" theory.

Vintage years 2000 and 2001 cumulative IRR measures are negative, but this might be expected following the "J" curve. The question is whether the decline in the stock market over the last three years will lengthen the time before the average cumulative IRR turns positive for vintage year 2000 and 2001 funds.

Exhibit 7 - Venture Exit Activity vs. S&P[14]

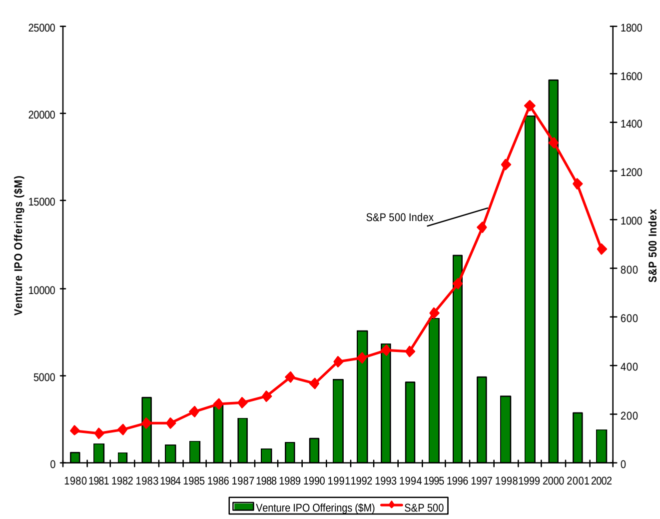


Exhibit 6 shows that the ideal time for a venture capital fund to invest is an estimated two to three years before a market upswing. Exhibit 7 shows when venture capital exits actually occurred, in terms of IPO activity. Just as there is an optimal time to get in, there is an optimal time to get out of an investment. Following the "buy low - sell high" principle, venture funds attempt to time the exit of their portfolio companies at market peaks.

However, as shown by the chart, venture IPOs tend to lag the market by about one or two years. When the S&P peaked in 1999, for example, venture IPOs peaked one year later. It is therefore possible that, following historic trends, once the current stock market rebounds, venture IPOs may follow one to two years later.

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[13] S&P Data derived from Commodity Systems Incorporated via Yahoo.com, using December monthly historical prices (symbol SPB) through 2002. Venture Vintage Year IRRs taken from Thomson Financial Venture Economics 2002 Investment Benchmarks Report, Page 39, Figure 3.002, Cumulative Benchmark Results as of December 31 2001 Overall Sample By Vintage Year.

[14] S&P Data derived from Commodity Systems Incorporated via Yahoo.com, using year end historical prices. Venture IPO data taken from Thomson Financial Venture Economics 2002 Investment Benchmarks Report, Page 353, Appendix C, U.S. Venture Capital Statistics.

2.3 SBIC Role in the Venture Capital Industry

While SBIC financings currently represent over 58% of actual venture financings[15], they represent only about 8% of all venture capital dollars (see Exhibit 2). Given the overall dollar impact, some observers have asked: Why do we need SBICs? What is the importance of SBICs to the venture capital industry? The answer lies in SBICs' unique ability to span the gap between start-up/early stage venture capital and larger venture transactions, and to reach a greater number and broader composition of small businesses through the leverage provided by the SBA.

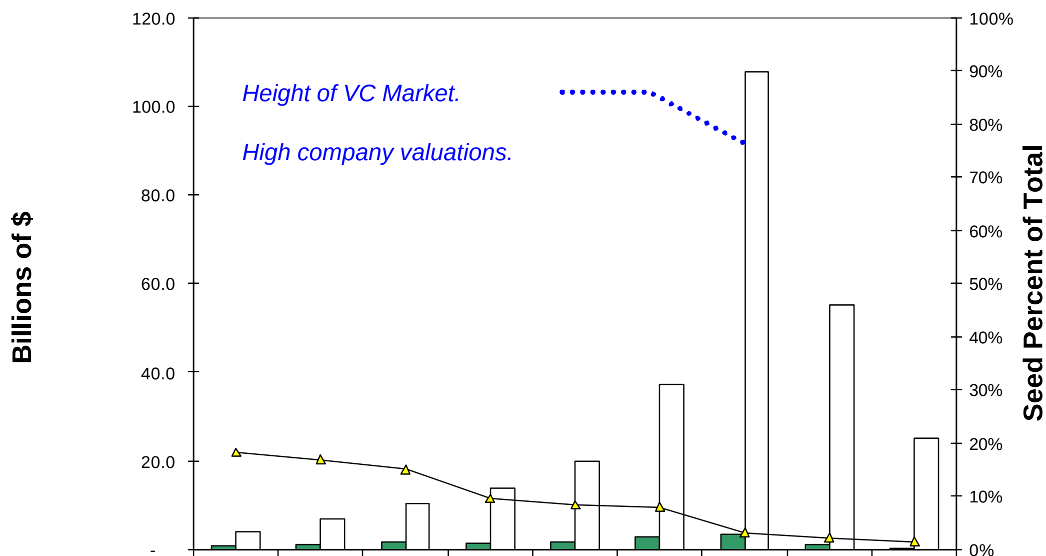
Filling the Gap in Private Equity. Because SBICs focus on small businesses, they naturally invest in more start-ups than the average venture capital fund, as shown in Exhibit 8 on the following page. The top chart shows total venture financing since FY 1994. The bottom chart shows the percentage of SBIC seed financing of venture seed during this same timeframe.

The top chart shows how venture financing dollars peaked in FY 2000 and that the overall contribution to seed stage financing has decreased since FY 1994, down to about 1% in FY 2002. The bottom chart shows that about 64% of all seed financing during this timeframe was performed by SBICs.

[15] Table 10 from SBIC Statistical Package February 2003, based on Calendar year 2002. Venture benchmark data utilizes VentureOne data from www.ventureone.com . SBIC data utilizes financings reported in FY 2002, not the date financings actually occurred. Each SBA Form 1031 (Portfolio Financing Report) is defined as one financing. VentureOne "financing" definition may be different.

Exhibit 8 – Comparison of Overall Venture and Seed Venture

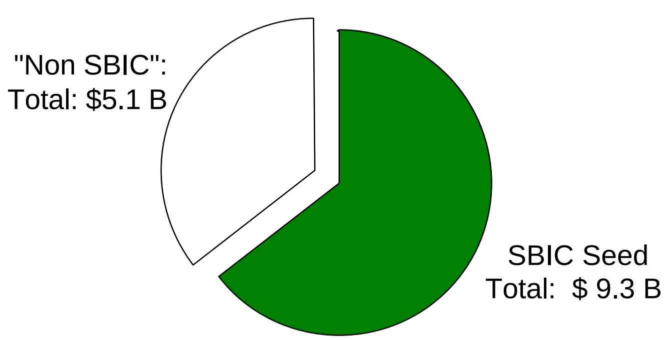
Venture Financing



	1994	1995	1996	1997	1998	1999	2000	2001	2002
Seed	0.7	1.2	1.6	1.3	1.7	3.0	3.4	1.2	0.4
Total Venture Financing	4.0	6.9	10.4	13.9	19.9	37.2	107.7	55.2	25.2
Seed % of Venture	18%	17%	15%	10%	8%	8%	3%	2%	1%

Seed Financing FYs 1994 through 2002

Venture Seed Total:
$14.4 Billion



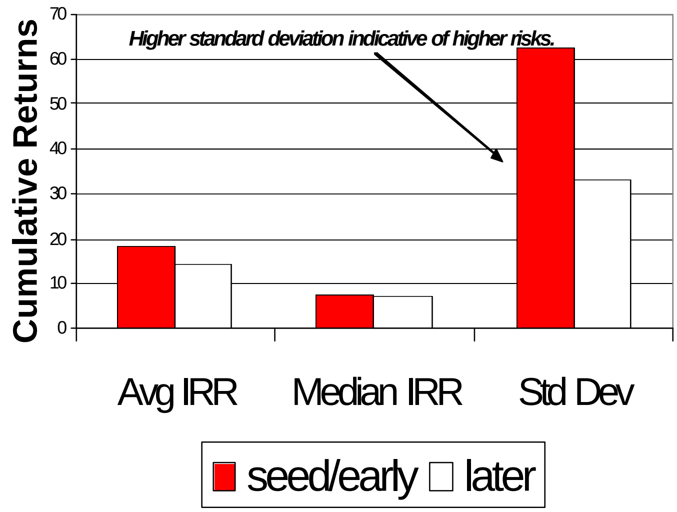
Notes:

- *The Investment Division does not currently characterize SBIC financings by funding stages (seed, early, later, etc). PWC's definition of seed is "The initial stage. The company has a concept or product under development, but is probably not fully operational. Usually in existence less than 18 months." The above SBIC "seed" financings were all financings of companies under 18 months old.*
- *All SBIC financings may not be part of PWC's survey group. Therefore, SBIC venture and seed financings may be greater than indicated.*
- *The Investment Division tends to receive reports on a fiscal year basis. Therefore, SBIC financings for FY 2002 will go up if new reports are received. It should be noted that other sources of venture capital information, including Venture Economics, PWC, and Venture One all have this same disclaimer and change data for time periods retroactively based on new data received.*

Influence of SBA Leverage in Attracting Private Capital. The gap in financing described above is not likely to be filled by non-SBICs, based on the fact that less than half a percent of non-SBIC venture capital dollars went into seed/start-ups in FY 2002. The reason is the risk/return ratio of seed and early stage investments compared to other transactions.

Exhibit 9 shows comparisons of seed/early stage funds with later stage funds. As shown, while the average IRR is higher for seed/early stage than later stage, the median IRR is almost the same. In fact, the standard deviation (a risk indicator) for seed/early stage is almost twice as high as later stage. Since money is invested on a risk and return basis, an investor might question whether the return on a start-up investment is commensurate with the risk.

Exhibit 9 – Venture Stage Comparisons[16]



(Cumulative Benchmarks through 2001 based on venture funds formed between 1969 and 2001)

How does SBA leverage work? An SBIC in good standing, with a demonstrated need for funds, may request leverage up to 200% of its private capital. The maximum amount of leverage varies according to the SBIC's private capital. To obtain leverage, SBICs issue debentures or participating securities, which are purchased or guaranteed by the SBA. Pools of these SBA-guaranteed debentures or participating securities are formed and sold to investors through a public offering. Under current procedures, debentures have a term of ten years, with semi-annual interest payments and a lump sum payment of principal at maturity. The ten-year debenture allows prepayment with penalty during the first five years and prepayment without penalty thereafter. The interest rate on the debenture is determined by market conditions at the time of the sale.

Participating securities are similar to debentures, however, the participating security provides for payment of dividends or interest and profit participation to SBA only when an SBIC has earnings. A unique feature of the participating securities is that SBA shares in the profits of the SBIC.

Exhibit 10 illustrates the benefits of this leverage to the SBICs and private investors. As shown, without SBA leverage, if the gross portfolio return were 35% (after management expenses and carried interest), the return to the investor would only be 25.2%. However, with SBA leverage, the returns would be 42.5%, commensurate with what private investors in a non-SBIC venture fund might expect given the risk.

SBA leverage provides the increased return potential that private investors demand for taking the risk of early-stage investing, thereby increasing the access to capital for small businesses that might not otherwise obtain financing.

[16] Venture data taken from Thomson Financial Venture Economics 2002 Investment Benchmarks Report, Page 303, Cumulative Benchmark Results Funds Formed 1969 to 2001 by Fund Stage Calendar Year..

Exhibit 10 – Impact of SBIC Leverage

Impact of SBIC Leverage

(Source: National Association of Small Business Investment Companies)

Gross Portfolio Return	Return to Investors without SBIC Leverage	Return to Investors with SBIC Leverage	% Yield Enhancement
10.0%	4.4%	0.0%	NA
15.0%	8.4%	12.7%	51.2%
20.0%	12.5%	19.5%	56.0%
25.0%	16.7%	27.3%	63.5%
30.0%	20.9%	35.2%	68.4%
35.0%	25.2%	42.5%	68.7%
40.0%	29.4%	49.6%	68.7%
45.0%	33.8%	56.2%	66.3%
50.0%	38.1%	63.7%	67.2%

Notes:

1) All returns refer to compound annual returns, i.e. IRR

2) Assumes returns are net of 2.5% annual expenses, 20% management carried interest, 15% uninvested capital, 4-year investment and 4-year holding period

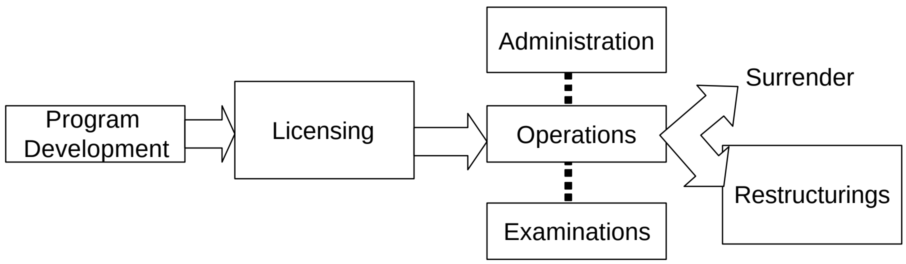
3) Assumed leverage: Participating securities (2X Private Capital), 7.75% Prioritized Payments and 9% Profit Participation Rate

2.4 Management and Oversight of the SBIC Program

In February 1992, an SBIC Investment Advisory Council, composed of members from the venture capital industry, the National Association of Small Business Investment Companies (NASBIC), and other stakeholders in the SBIC program, submitted a report to the SBA Administrator regarding the SBIC Program. One of the findings of this report stated, "Perhaps the most important lesson is the need to match authority with responsibility, and to establish long-term accountability at all levels of the SBIC management process." Because the government guarantees the funds used in the SBIC program, the SBA holds a fiduciary responsibility to ensure that SBICs utilize these funds in the best interest of the taxpayer. The SBA's Investment Division provides the necessary oversight for this program.

Exhibit 11 depicts the typical process for obtaining an SBIC license and the lifecycle of an SBIC as it moves through the various oversight functions of the Investment Division. As indicated, SBIC Program Development screens applicants and conducts preliminary evaluations of prospective SBIC venture fund management teams and their proposals. Once they pass initial hurdles, SBIC applicants then face a rigorous licensing process. If they receive their license, they are transferred to the Office of SBIC Operations. The Offices of SBIC Administration and SBIC Examinations play key roles during this timeframe. At the end of a fund's life (typically ten years), the SBIC surrenders its license if it was not previously transferred to the Office of SBIC Liquidations. Further detail regarding each step and the related office are described below.

Exhibit 11 – SBIC Program Lifecycle



SBIC Program Development. One of the recommendations from the 1992 SBIC Program Study was to "Establish a Marketing/Business Development function reporting to the Associate Administrator for Investment (AAI) to sell the SBIC program nationally to potential new sources of private capital and prospective management teams." Program Development, under the Office of Chief Administrative Officer, performs this function. This team looks for venture management teams with established track records in venture capital. Program Development ideally looks for the following attributes in SBIC candidates:

- Private equity experience relevant to proposed fund
- Investment experience as a principal rather than an agent (i.e., investment banker, consultant, broker)
- Realized track record of superior returns relative to 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

Candidates going through Program Development typically follow these steps:

- Management Assessment Questionnaire ("MAQ"): This comprehensive evaluation form is a series of structured questions concerning management's plans for the prospective SBIC and the detailed experience and qualifications of the management team.

- Analyst Review and Preliminary Due Diligence: Once the MAQ is submitted, the Investment Division assigns a program development specialist to the case. The specialist works with the applicant to clarify and analyze the MAQ in detail, especially with regard to the applicant's strengths and weaknesses, and performs initial due diligence.

- Preliminary Investment Committee Review: Generally, within one to two months, the assigned staff person makes a recommendation to the Investment Committee of Investment Division (composed of senior members of the Division) whether to invite the principals to the SBA for a formal interview.

- Investment Committee Presentation: If the initial impression and supporting documentation and due diligence show that the management team may be qualified for a license, the entire team is invited to an interview with approximately 7-15 SBA personnel in attendance. This allows the applicant to expand on their strengths and discuss any weaknesses identified through the MAQ.

- Assessment: After the interview, the Investment Committee decides whether or not to issue a "go forth letter," which moves the applicant into a more rigorous licensing phase. A go-forth letter does not mean that the SBA has determined that the applicant qualifies to receive an SBIC license, only that they qualify for further consideration and due diligence.

Licensing. Another recommendation of the 1992 SBIC Program Study was, "Establish stringent new licensing regulations and standards, and allow the SBA to reject applications for licenses when those standards are not met." The study noted that as of 1992, "…the SBA hasn't declined many license applications over the SBIC program's 30-year history" and "Had the SBA felt secure in its authority to decline license applications, some of the SBA's exposure to loss might have been avoided." Since licensed SBICs hold the investment decision, management, and oversight of the SBA-guaranteed funds, ensuring that only qualified applicants are licensed is critical to minimize potential financial losses of the program.

The Office of Licensing and Program Standards holds this crucial responsibility:

- License Application and Private Capital Commitments: The applicant must raise so-called "regulatory capital" in the form of commitments from private sources. Prior to filing its license application, the applicant is required to raise a minimum private capital commitment of $5 million for a debenture fund, and $10 million for an equity, or so-called "participating securities" fund. A minimum of 30% of this capital must come from sources unaffiliated with the fund management.

- Analyst Review: The Office of Licensing assigns a lead analyst to review each application. The analyst performs an in-depth review of the application, business plan, financial projections, legal documentation and final due diligence on the management team. When the review is complete, the applicant then undergoes three levels of approval before actually receiving its license.

- Divisional Approval: The lead analyst presents the application to the Investment Division Licensing Committee, which generally meets on a monthly basis. This committee is composed of senior managers of the Investment Division.

- Agency Licensing Approval: If Divisional Licensing approves the application, it is then presented to the Agency Licensing Committee, which is composed of certain senior managers of the SBA.

- SBA Administrator Final Approval: Finally, if the Agency Licensing Committee approves, the application is submitted to the SBA Administrator for final approval. If signed, the applicant receives an SBIC license and is transferred to the Office of SBIC Operations.

Operations. The 1992 SBIC Program study noted the importance of continuous monitoring of the SBICs' portfolios, in terms of "clear and timely analysis of financial statements," "…balance sheet, cash flow and income statement analysis with particular emphasis on key indicators of potential problems in SBICs, and " .. spotting potential problems early." The study's emphasis was to maintain a relationship such that potential problems could be identified early to give time for SBIC management and the Investment Division to work towards possible solutions. The Office of SBIC Operations addresses these concerns through its oversight.

The Director of SBIC Operations is responsible for regulatory and financial oversight, and leverage (funding) to the SBICs. Each licensee is assigned an operations analyst who serves as their primary contact. The operation analyst is responsible for the analysis of all financial statements, examinations, and investigation reports covering the operations and practices of individual SBICs. In addition, the analyst evaluates the financial stability and reliability of the SBICs, and their compliance with the Small Business Investment Act of 1958, as amended, and other related rules and regulations.

Administration. The 1992 SBIC Program study stressed the importance of data collection and analysis, suggesting "simple off-the-shelf financial reporting models and analytical software" and "quarterly financial reporting… in a format that most closely resembles a venture capital fund's normal quarterly reporting, with additional data provided annually to the Agency on companies backed, and jobs, wealth, and taxes created." Data Management provides this responsibility as part of the Office of Chief Administrative Officer. In addition, Funding Administration as part of this office directs, administers, and coordinates the periodic pooling and funding of both SBIC debentures and participating securities for the program.

Examinations. The 1992 SBIC Program Study also recommended, "The examination function provided in Section 310 of the Small Business Investment Act should be returned to the Investment Division to assure control over the frequency, scope, and performance of compliance exams." The intent of this recommendation was to put the responsibility back in the program office directly responsible for administering the program.

The Office of SBIC Examinations plans, directs and coordinates the Agency's program for examining SBICs that operate under the provisions of the Small Business Investment Act of 1958, as amended. Primary goals of examinations include:

- Determining whether licensees are complying with the Small Business Investment Act and implemented regulations;
- Assessing the financial condition of licensees and SBA's financial vulnerability; and
- Ensuring the accuracy of information that licensees submit to SBA.

The Office of SBIC Examinations is headed by a Director in the Washington headquarters, and supported by 29 examiners in six field offices. Examiners independently gather and report factual information to the Office of SBIC Operations, so that the Office of SBIC Operations can monitor and regulate the activities of the licensees.

Liquidations. The Office of SBIC Operations proactively monitors the SBICs to determine as soon as possible any possible problems in the portfolio. If severity of problems warrants action, the operations analyst recommends transfer of the SBIC into "Restricted Operations" mode (for participating securities SBICs). If the severity of the fund's condition worsens, the Office of SBIC Operations may recommend transfer of the SBIC to the Office of SBIC Liquidations. For debenture SBICs, the process is less complex: when an SBIC defaults, it is usually transferred directly to the Office of Liquidations. (In some instances, the note may be put on "demand" and the SBIC will continue in the Office of Operations.)

The Office of SBIC Liquidations' primary goal is to maximize the net recoveries in an appropriate amount of time on these SBICs, while recognizing the interests of other parties affected (i.e., small business concerns funded by SBICs) and furthering program integrity. The Office of SBIC Liquidations manages, oversees, and takes necessary action on behalf of SBA, both as creditor and as Receiver.

Surrender. The Office of SBIC Liquidations is neither the typical nor preferred way for an SBIC to exit the program. Usually, the SBIC requests approval to surrender its license, accompanied by an offer of immediate repayment of all outstanding leverage (including any prepayment penalties thereon), or by a plan satisfactory to the SBA for the orderly liquidation of the Licensee. An SBIC may not surrender its license without SBA's prior written approval.

3. Benefits of the SBIC Program to the U.S. Economy

In 2001, the National Venture Capital Association (NVCA) commissioned a report conducted by DRI-WEFA to evaluate the economic benefits of venture capital. The DRI-WEFA report[17] highlighted the following:

- ***Economic Growth and Job Creation***: In 2000 alone, companies backed with venture capital funding between 1980 and 2000 contributed nearly $1.1 trillion to the U.S. gross domestic product (GDP) – 11% of the GDP – and employed 12.5 million people.

- ***Geographic Coverage***: The study shows that venture capital flows throughout all geographic regions of United States.

- ***Business Productivity***: The study noted higher productivity in terms of sales, taxes, exports, and R&D as well as a strong correlation between venture capital activity and gross state product.

- ***Technology and Innovation***: Venture capital "lubricates the wheels of innovation." The study looked at companies across industries using three metrics to measure innovation: patents, imitating companies, and product lines.

As a subset of the overall venture capital industry, the SBIC Program produces measurable benefits to the United States in ***all*** of these important areas. The following sections describe those results in detail. Our analysis generally starts in FY 1994, when the Participating Securities program was created and when the impact of equity investing can begin to be measured.

[17] The Economic Impact of the Venture Capital Industry on the U.S. Economy, conducted by DRI-WEFA on commission from the National Venture Capital Association, June 2002.

3.1 SBIC Contribution to Economic Prosperity and Employment

The SBIC program plays a major role in the U.S. economy, providing jobs, revenues, and taxes throughout the United States. The exciting potential of an SBIC investment is how it can turn into jobs, revenues, and taxes on a much larger scale, thereby encouraging U.S. economic expansion and growth.

Job Creation and Retention. We can measure both short and long-term employment impacts attributable to SBIC financings. Because venture capital often provides long-term growth capital for a company, it is difficult to ascertain the exact impact. The SBA currently has three different ways to look at jobs: 1) Utilizing the NVCA industry ratio; 2) Number of jobs from pre-financing numbers (from Form 1031s); 3) Number of jobs in companies held in SBIC licensee portfolios (from Form 468). Information from the last two data sets tends to be incomplete, and in the case of the Form 468, unaudited. Disclaimers regarding this data are provided with the analysis.

> ***Using NVCA's industry ratio[18], SBIC total financings reported in FY 2002 of $2.7 billion[19] yielded over 73,000 jobs.***

In October 2001, the NVCA issued a press-release indicating that venture capital-backed companies directly employed over 7.5 million jobs in calendar year 2000. This number includes all companies that received venture capital (totaling $1.3 trillion) from 1970-2000. The press release stated, "…research shows that one American job existed in 2000 for every $36,000 dollars of venture capital invested over the last three decades."[16] Since this press release, NVCA has released the final report that indicates that 12.5 million jobs can be attributed to venture capital investment. However, the SBA utilizes the previous $36,000 number because it is more conservative.

While no similar study on SBICs has been conducted, using this ratio, the SBA calculates that approximately 73,000 jobs existed based on financings reported in FY 2002 ($2.7 billion).

FOOTNOTE: (Disclaimers to Estimate: 1) The Investment Division recognizes that all financings may not be considered venture financings due to the lack of equity components in some financings; therefore, the estimate may not be statistically reliable. 2) The Investment Division has not seen the details of the DRI-WEFA study, so inaccuracies based on misinterpretations of data may have occurred. 3) While timings of financings play an important factor in this derivation, because of lack of information regarding the study, timing was disregarded.)

[18] "Three Decades of Venture Capital Investment Yields 7.6 Million Jobs and $1.3 Trillion in Revenue - Research Finds That $36K of VC Investment Creates a US Job", NVCA October 22, 2001 Press Release, on NVCA.org website.
[19] This number is derived from Licensees reports of small business financing information to the Investment Division, not on the date of financing. This number includes all financings, including debt, debt-equity, and equity.

SBIC financings from FY 1994 through FY 2002 supported companies which prior to SBIC financing employed a total of over 920,000 employees in all 50 states plus Puerto Rico and the District of Columbia.[21]

Exhibit 12 – Total Employees of Companies Receiving SBIC Financing (FY 1994-2002)[21]

Based on Unaudited Data

(In Descending Order of Employees and indicating % of Labor Force in Each State[20])

State	Employees	% Labor
CA	148,510	0.9%
NY	83,765	1.0%
TX	75,413	0.8%
NC	52,558	1.4%
FL	51,599	0.7%
OH	40,755	0.7%
NJ	40,276	1.0%
MA	37,388	1.2%
PA	35,868	0.6%
MI	27,690	0.6%
TN	26,115	1.0%
GA	25,389	0.6%
IL	22,650	0.4%

State	Employees	% Labor
KS	20,516	1.5%
CO	17,664	0.8%
MN	17,583	0.7%
WI	16,784	0.6%
CT	16,354	1.0%
IN	14,964	0.5%
MO	14,376	0.5%
VA	14,101	0.4%
LA	13,304	0.7%
WA	12,829	0.4%
AZ	9,876	0.4%
MD	9,598	0.4%
Others	75,072	
Total	920,997	

*Note: While SBICs financed companies in all states, plus the District of Columbia, Puerto Rico, and the Virgin Islands, only the top 25 states in terms of pre-financing employee numbers as reported on the Form 1031s are detailed above. All other states are grouped together under "Others" in order to protect privacy information that may be identifiable. The data is unaudited and self-reported by the SBICs.

FOOTNOTE: It should be noted that employee number representation is based on where the company is located, as actual employee residency data is not available.

One of the limitations with this number is it only shows the numbers of jobs prior to financing, not after financing. Also, since this only includes financings, acquisitions and mergers, as well as previously held portfolio companies are not considered. By looking at the Annual 468 (Statement of Financial Position) Report's economic schedule, all companies in which an SBIC currently holds an interest can be considered.

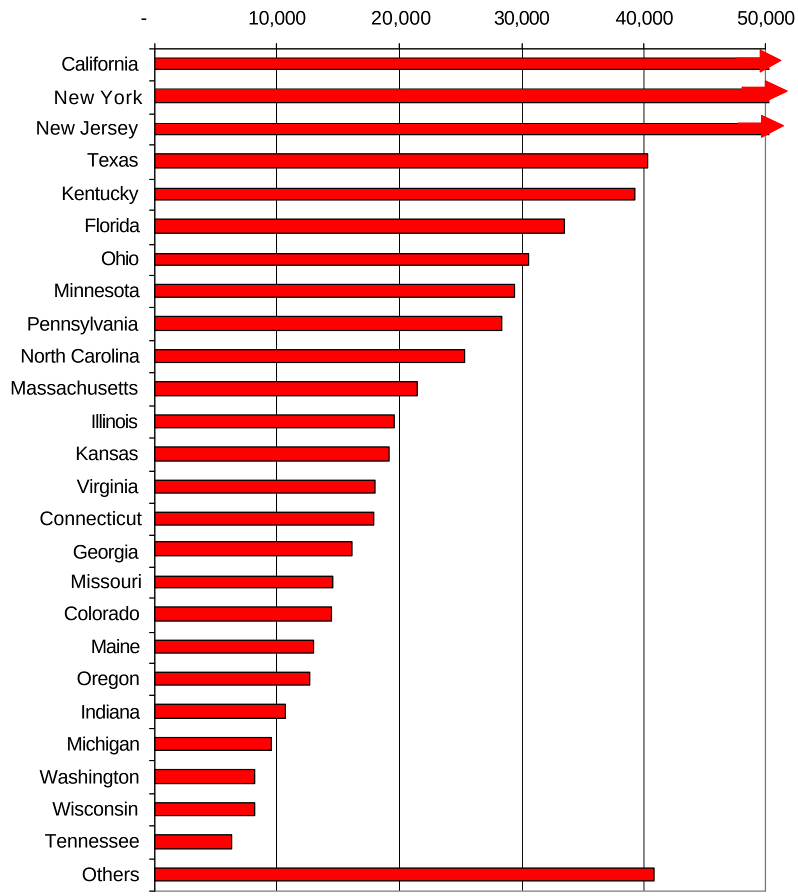
[20] *Labor data taken from U.S. Labor and Bureau Statistics report for 2000 census, using both part-time and full-time workers.*

[21] *This data was based on all financings taken place between FY 1994 and FY 2002 reported on Form 1031s as pre-financing data, as received by Data Management. Since companies often receive multiple financings, only the last reported financing data for the company was used. It should be noted that only 53% of the distinct companies filled in their employee number over this set of data. Since only reported numbers were used, this figure may be low. The data is unaudited and self-reported by the SBICs.*

Over 1.1 million people – representing 9% of venture-backed companies – were employed by companies in which SBICs maintained a financial interest in FY 2002.

Exhibit 13 – Employees in Companies in Which SBICs Held a Financial Interests in FY 2002 Reporting

(Based on Unaudited Data)



StateText	Jobs
California	406,572
New York	115,777
New Jersey	64,949
Texas	40,330
Kentucky	39,289
Florida	33,599
Ohio	30,537
Minnesota	29,431
Pennsylvania	28,317
North Carolina	25,399
Massachusetts	21,423
Illinois	19,624
Kansas	19,143
Virginia	18,070
Connecticut	17,880
Georgia	16,099
Missouri	14,601
Colorado	14,406
Maine	12,927
Oregon	12,643
Indiana	10,623
Michigan	9,506
Washington	8,249
Wisconsin	8,243
Tennessee	6,337
Others	40,870
Total	1,064,844

Notes:

1) While companies in which SBICs held an interest in FY 2002 existed in all states, plus the District of Columbia, Puerto Rico, and the Virgin Islands, only the top 25 states in terms of job numbers as reported on the Form 468s were identified above. All other states are grouped together under "Others" in order to protect privacy information that may be identifiable.

2) This data was retrieved from the schedule database provided by Data Management. The schedule database is based on Form 468 that each SBIC is required to submit to SBA on an annual basis. The data is not audited. It should be noted that only 35% of the companies represented on the 468 form contained employee data, as the licensees do not always complete the form. Since multiple records exist for each company, only the last record was used to identify the above data to avoid double-counting of figures. Companies are identified by their employer ID number, when available. When unavailable, the employer name was used to identify the company. In addition, SBIC Licensees may have used data from previous years to provide estimated figures. Data entered previous to 2000 was removed from the above chart. Only one third of the data was within the 2000 and above range. Of those licensees in the 2000 and above range approximately 10% did not provide employee data. It should also be noted that this analysis disregards percentage of ownership by the SBIC. It should be noted that employee number representation is based on where the company is located, as actual employee residency data is not available.

Exhibit 14 –Unaudited Economic Data from SBA Form 468 as Received in FY2002[22]

(Based on Unaudited Data)

StateText	Jobs	Federal Taxes	State & Local Taxes	Gross Revenues
California	406,572	2,679,039,845	283,930,996	108,455,277,290
New York	115,777	358,588,161	148,368,056	11,654,963,135
New Jersey	64,949	196,328,246	33,606,179	4,577,284,134
Kentucky	40,330	275,821,337	30,359,209	5,789,753,760
Texas	39,289	70,849,953	22,011,448	1,886,155,931
Florida	33,599	261,284,402	29,651,607	3,343,568,151
North Carolina	30,537	127,505,989	40,004,121	3,904,293,602
Pennsylvania	29,431	61,658,720	19,551,908	3,943,222,418
Ohio	28,317	185,210,897	42,797,849	3,776,566,285
Minnesota	25,399	92,060,851	41,699,598	4,361,031,189
Illinois	21,423	274,283,209	81,583,642	3,027,515,257
Colorado	19,624	131,562,139	27,947,904	2,712,765,858
Connecticut	19,143	52,382,322	27,710,009	1,591,981,800
Kansas	18,070	106,400,400	29,489,181	1,764,947,916
Missouri	17,880	93,617,246	24,217,593	2,806,081,729
Massachusetts	16,099	110,235,820	28,653,172	2,742,337,232
Virginia	14,601	69,489,709	19,908,429	2,078,859,486
Oregon	14,406	84,933,768	22,478,824	974,687,950
Georgia	12,927	51,041,819	14,508,813	2,316,102,457
Maine	12,643	95,721,728	16,454,491	2,122,542,013
Indiana	10,623	54,813,110	18,420,721	1,500,136,517
Michigan	9,506	55,026,701	17,829,107	1,833,266,516
Washington	8,249	65,714,516	4,691,422	1,400,313,104
Maryland	8,243	35,759,069	12,302,622	1,739,503,114
Wisconsin	6,337	51,007,240	10,146,198	1,767,041,332
*All others	40,870	268,834,348	70,565,253	6,931,439,388
Total	1,064,844	5,903,037,313	1,116,397,147	187,440,155,355

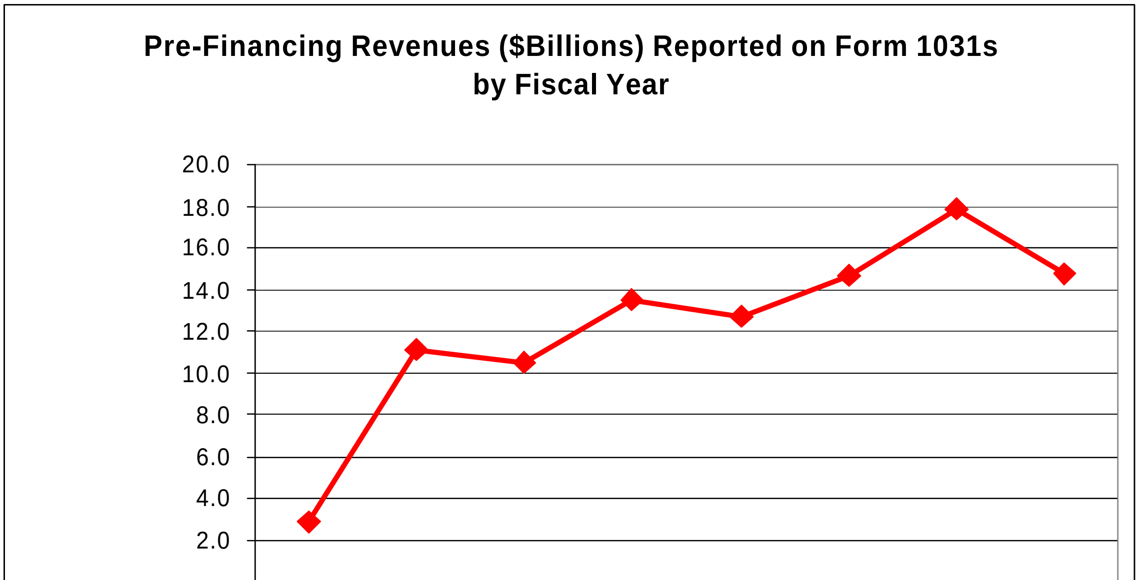
*Note: While companies in which SBICs held an interest in FY 2002 existed in all states, plus the District of Columbia, Puerto Rico, and the Virgin Islands, only the top 25 states in terms of job numbers as reported on the Form 468s were included. All other states are grouped together under "All others" in order to protect privacy information that may be identifiable.

[22] This data was retrieved from the schedule database provided by Data Management. The schedule database is based on Form 468 that each SBIC is required to submit to SBA on an annual basis, including both leveraged and non-leveraged funds. The data is not audited. Since multiple records exist for each company, only the last record was used to identify the above data to avoid double-counting of figures. Companies are identified by their employer ID number, when available. When unavailable, the employer name was used to identify the company. In addition, SBIC Licensees may have used data from previous years to provide estimated figures. Data entered previous to 2000 was removed from the above chart. Only one third of the data was within the 2000 and above range. Of those licensees in the 2000 and above range approximately 10% did not provide employee data, about 14% did not provide revenues, and about 84% did not include federal taxes. It should also be noted that this analysis disregards percentage of ownership by the SBIC and that employee number representation is based on where the company is located, as actual employee residency data is not available.

Revenues. Similar to the substantial impact on jobs, SBICs supported overall U.S. productivity throughout the United States throughout the years of this program.

> ***Pre-financing revenues for companies financed by SBICs reported in FY 2002 totaled approximately $14.8 billion.***

Exhibit 15 – Pre-Financing Revenues ($B) Reported on Forms 1031s by Fiscal Year



	FY 1995	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002
Revenues ($B)	2.9	11.1	10.4	13.5	12.7	14.7	17.9	14.8

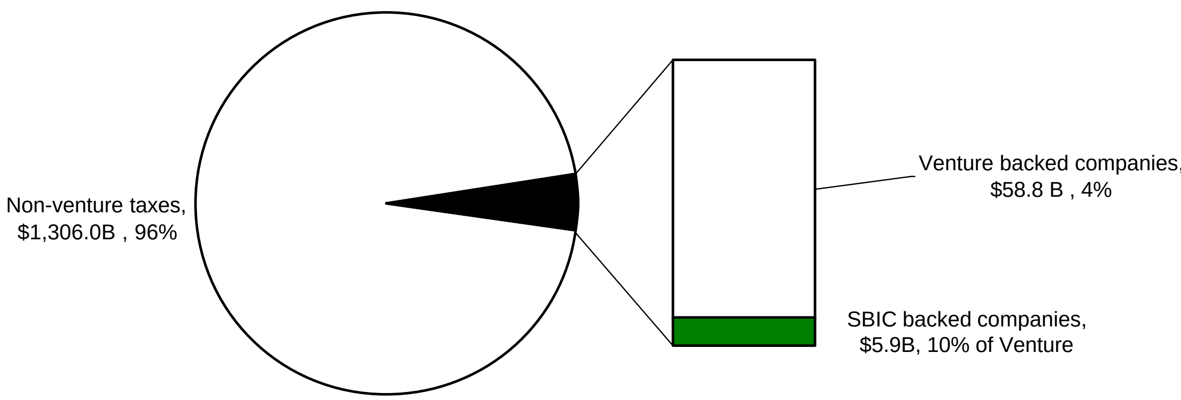
Note: This data was retrieved from SBIC Annual Statistical Packages from FY 1996 through FY 2002, from the table entitled "Financial Information on Businesses Financed."

Income Taxes. One of the largest benefits American taxpayers receive as a result of SBIC investments comes in the form of federal taxes paid by SBIC-backed companies and their employees.

In FY 2002 alone, companies in which SBICs held a financial interest paid and/or withheld federal taxes of almost $6 billion – approximately 10% of total venture-backed company taxes.

Exhibit 16 – Federal Tax Dollars in Billions of Dollars (Individual and Corporate)

(Based on Unaudited Data)



Notes: Total tax dollar figure (individual and corporate) retrieved from IRS website for the year 2000. The venture backed tax dollars are based on the DRI-WEFA report for the year 2000. SBIC backed tax dollars were taken from 468 schedule data as reported by the SBICs in FY 2002. This data was retrieved from the schedule database provided by Data Management. The schedule database is based on Form 468 that each SBIC is required to submit to SBA on an annual basis. The data is not audited. Since multiple records exist for each company, only the last record was used to identify the above data to avoid double-counting of figures. Companies are identified by their employer ID number, when available. When unavailable, the employer name was used to identify the company. In addition, SBIC Licensees may have used data from previous years to provide estimated figures. Data entered previous to 2000 was removed from the above chart. Only one third of the data was within the 2000 and above range. Of those licensees in the 2000 and above range approximately 84% did not include federal taxes or the taxes were identified as zero. It should also be noted that this analysis disregards percentage of ownership by the SBIC.

In FY 2002 alone, federal income taxes paid by companies in which SBICs had a financial interest and their employees -- $5.9 billion.

FOOTNOTE: Per Table 32 of the SBA Statistical Package, February 2003, the SBA leverage issued through debenture and participating security poolings totaled $5.7 billion. Per Exhibit 16 shown above, federal tax dollars totaled $5.9 billion from companies in which SBICs had a financial interest. See Exhibit 16 disclaimer notes with regard to these figures.

> ***Companies in which an SBIC held a financial interest paid state and local taxes paid taxes of over $1 billion, as compared to venture-backed companies paying $7.8 billion in the year 2000.***

FOOTNOTE: Per Exhibit 14, data retrieved from the FY 2002 468 unaudited schedule database indicated that approximately $1.1 billion was paid in state and local taxes from companies in which SBICs held an interest. See Exhibit 14 disclaimer notes with regards to this data. Per the DRI-WEFA study, venture-backed companies paid $7.8 billion in state and local taxes in the year 2000.

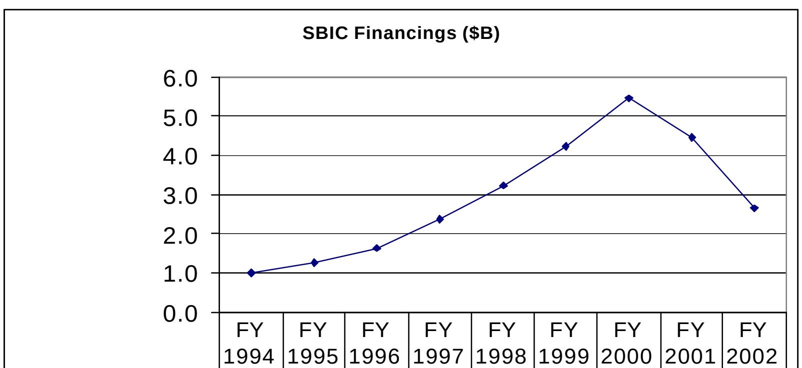
3.2 Geographic Reach.

All 50 states plus the District of Columbia, the Virgin Islands and Puerto Rico have benefited from the SBIC Program. While traditional venture capital provides similar coverage, as the numbers show, SBICs often reach different areas and provide special benefits to low and middle income areas.

> ***SBICs provided over $26 billion in financings from FY 1994- 2002, covering all 50 states, the District of Columbia, Puerto Rico, and the Virgin Islands.***

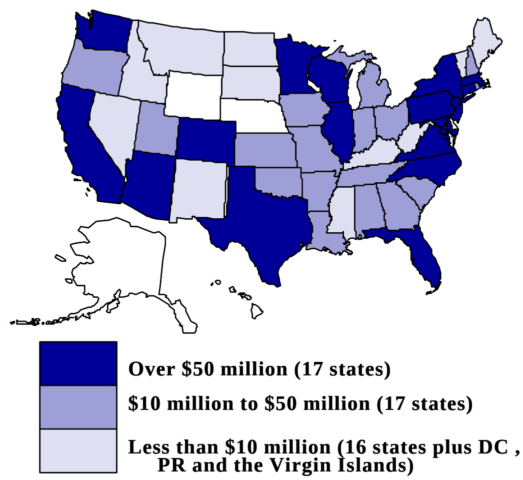
Exhibit 17 – SBIC Reported Financings ($B)

Reported Financings FYs 1994 through 2002



	FY 1994	FY 1995	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002
Financing ($B)	1.0	1.2	1.6	2.4	3.2	4.2	5.5	4.5	2.7

FY 2002 Financings: $2.7 B

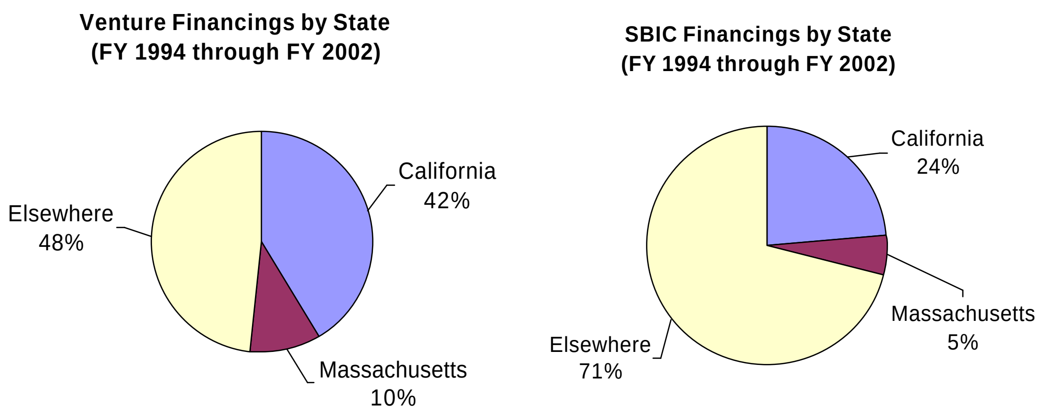


**Notes: Data derived from Table 2and Table 7 chart from SBIC Statistical Package dated February 2003. Financings reflect when they were reported, not when financings actually occurred.*

SBICs provide more even financing distribution across states than venture capital as a whole.

Since SBICs were only 8% of Venture Capital Financing dollars during FY 1994 through FY 2002, in order to perform a comparison on geographic distribution, the percentage of financing dollars to each state was compared. While venture capital is represented throughout the country, many less populated states receive fewer financing dollars. Venture capital tends to be concentrated in California and Massachusetts. Exhibit 18 compares percentage of financings per state for California, Massachusetts, and all other states, plus the District of Columbia.[23]

Exhibit 18 - Percentage of Financings Dollars per State for All Financings FYs 1994 through 2002



**Notes: Venture statistics based on Venture Expert/MoneyTree financing numbers for FY 1994-2002. SBIC statistics were taken from Form 1031 financing data Both numbers are based on disbursement/financing dates.*

- The top two venture funded states (California and Massachusetts) received over 51% of venture financing during this period. A presentation from PriceWaterhouseCooper/NVCA indicated that in calendar year 2002 venture capital performed almost 45% of their financings in California and 13% in New England.[24]

- 26 states received less than .3% of all venture financing.

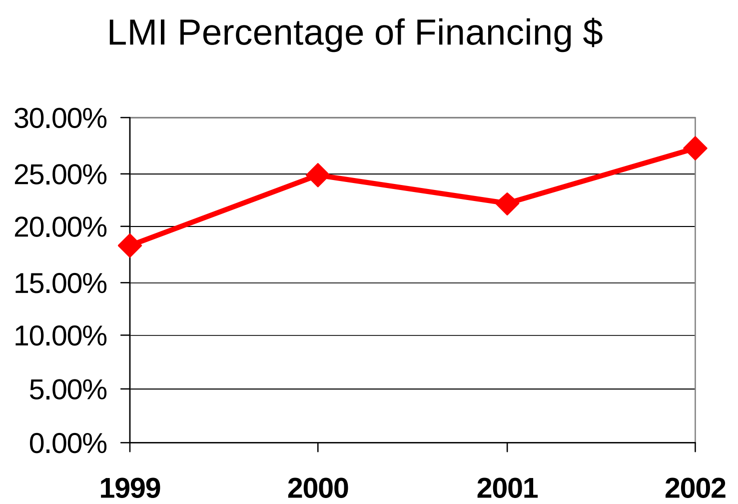
- In seven states, SBIC funding provided 50% or more of venture funding to companies in each state during this timeframe.

[23] Since financings for venture capital in Puerto Rico and the U.S. Virgin Islands were unavailable, they were excluded from this comparison analysis.
[24] PricewaterhouseCoopers/Venture Economics/National Venture Capital Association MoneyTree™ Survey Borie Q4'02 SF MoneyTree.ppt

SBICs provide a significant amount of financing to low and moderate income (LMI) zones, with a record high of over 27% of all financing dollars reported by the SBICs in FY 2002.

The exhibit below shows financings reported by the SBICs in the indicated FYs. (Financing data, categorized by LMI zone, was only available for the FYs 1999 through 2002.)

Exhibit 19 – LMI Percentage of SBIC Financing Dollars by Reporting Date (FYs 1999 through 2002)



Financings in Millions of $	1999	2000	2001	2002	Totals
LMI Financing $	771	1,352	988	725	3,835
Total Financing $	4,221	5,466	4,455	2,660	16,802
% LMI of Total	18.26%	24.73%	22.17%	27.26%	22.83%

Notes: Data derived from 1031 tables maintained by Data Management through FY 2002 and from Low Income Report, Numbers reflect when financing were reported,* ***not* *when they occurred. Therefore, financings may have occurred in earlier FYs than reported*

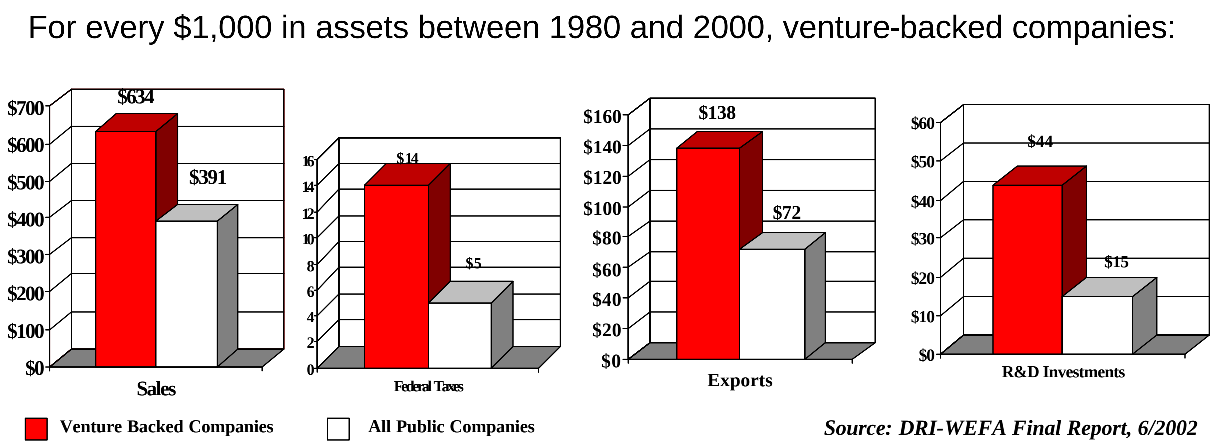
.

3.3 Business Productivity

The DRI-WEFA study noted a higher productivity in terms of sales, taxes, exports, and R&D as well as a strong correlation between venture capital activity and gross state product.

> ***Companies funded by venture capital between 1980 and 2000 generated more sales, paid more taxes, generated more exports, and invested more in R&D than public companies on a comparative basis for every $1000 in assets (Exhibit 20).***

Exhibit 20 – Venture-Backed Companies Produce More Sales, Pay More Taxes, Generate More Exports, and Invest More in R&D than Public Companies

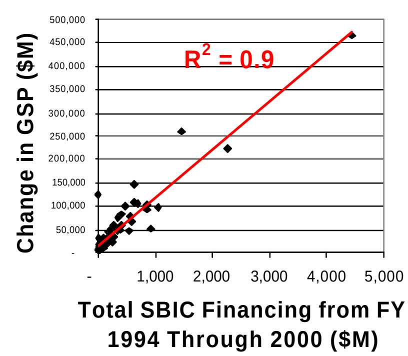


Source: DRI-WEFA Final Report, 6/2002

SBIC financing is strongly correlated to growth in Gross State Product (GSP).

The exhibit to the right plots growth in GSP by state from 1994 through 2000 and the related SBIC financings. As shown, there is a very strong correlation, as noted by the R-squared, the Pearson product moment correlation coefficient of ".9". (Perfect correlation is indicated by "1".) While there appears to be a strong correlation, there has been no study to determine whether SBIC financings cause an increase in GSP, if SBICs tend to finance where the GSP is growing, or there is any cause-effect relationship between financings and GSP growth.

Exhibit 21 – Correlation of SBIC Financings to Change in GSP between FY 1994-2000[25]



[25] GSP data retrieved from http://www.bea.doc.gov. Note that GSP was only available on calendar year basis only.

3.4 SBIC Technology/Innovation

In addition to the measurable economic benefits of the program related to productivity and job creation, SBICs provide important contributions to U.S. technology research, development and innovation.

Technology Research & Development ("R&D"). When a company cuts R&D spending, short-term profits may improve but the company's long-term growth stands at risk. R&D spawns new products, new science, and new solutions to keep companies competitive in the marketplace. Corporate R&D spending is critical to the United States to maintain our competitive edge in the global market.

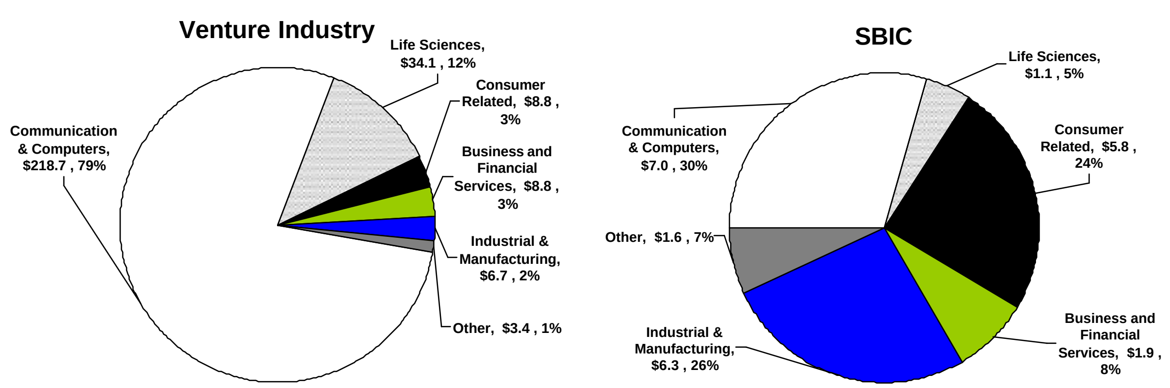
SBIC financings promote corporate spending in Research and Development

The DRI-WEFA study on venture capital noted that for every $1 invested in companies during 1970-1999, these companies invested $1 in R&D in 2000. While not all dollars in the SBIC program are considered venture investments, it is reasonable to assume that SBIC financings provide similar benefits.

SBIC invest not just in "high tech" and life science, but consumer related, manufacturing, and other business innovations

As shown in the chart below, total venture capital and SBIC financings between FY 1994-2000 heavily support not just information technology (of which $7 billion came from SBICs), but also life sciences (of which $1.1 billion came from SBICs), manufacturing, and other industries.

Exhibit 22 – Comparison of Financing Distributions by Industry for FY 1994-2000



****Notes:***

1. *Venture Capital data was taken from VentureExpert database.*
2. *SBIC data was retrieved from Form 1031 tables, as provided by Data Management.*
3. *Financings are based on when financings/disbursals took place.*
4. *Only financings with equity features were included.*
5. *VentureExpert categorizes industry by definitions not directly related to NAIC or SIC categories used by the SBICs. SBICs prior to 1997 utilized SIC codes and NAIC codes were again changed in 2002. The Investment Division converted all companies to NAIC 2002 codes and then created a mapping based on VentureExpert category definitions to create benchmark shown. SBICs were responsible for original coding, either SIC or NAIC.*

Innovation. By providing high risk financing, venture capital promotes and supports innovation across industries and geography.

Point 1: Venture Capital and the SBIC Program promote innovation.

The DRI-WEFA Study noted how venture capital spurs innovation across all industries as measured by patents, imitating companies; and product lines. A study[26] published in Rand Journal of Economics by Samuel Kortum (Boston University) and Josh Lerner (Harvard University) confirms this theory, stating that,

> *"… venture funding does have a strong positive impact on innovation. The estimated parameter varies according to the techniques we employ, but focusing on a conservative middle ground, a dollar of venture capital appears to be about **three times** more potent in stimulating patenting than a dollar of traditional corporate R&D."*

While no separate study has been performed on SBICs, it is reasonable to assume that a similar relationship exists. A recent study (February 2003) by Diana Hicks of CHI Research, "Small Serial Innovators: The Small Firm Contribution to Technical Change," indicated that "*Smaller firm patents were cited in subsequent patent applications 28 percent more often than those of larger firms and were twice as likely to be among the one percent most cited patents*." Since SBICs concentrate on smaller firms, the study supports this assumption.

[26] Kortum, Samuel and Lerner, Josh, "Assessing the Contribution of Venture Capital to Innovation," *RAND Journal of Economics*, Vol. 31, No. 4, Winter 2000,pp. 674–692

Point 2: Venture Capital and the SBIC program have spurred innovation across industries.

While innovation is often more measurable (via patents) in high technology industries, SBICS and Venture Capital recognize that ideas and improvements occur across industries. As noted in the DRI-WEFA study, the venture capital industry boasts companies throughout all industries including, Airgas, Amazon.com, Boise Cascade Corporation, Costco, Dell, Fischer Scientific International, FMC Corporation, Mellon Financial, and Worldcom. Similarly, the SBIC program also has a long list of successful companies at one time backed by SBIC financing throughout industries, including those in the table below.

Companies that Received SBIC Funding

Industry	Company	Revenues (in $billions)	Employees
Transportation	Federal Express	20.6	184,953
Computers	Sun Microsystems	12.5	39,100
	Apple Computer	5.7	10,211
Other Technology	Harman International Ind.	1.1	10,389
	Orbital Sciences Corporation	0.6	1,800
Internet	America On-line	41.1	89,300
Software	Peoplesoft	1.9	8,293
	Kronos	0.3	2,200
Business Services	Labor Ready, Inc.	0.9	2,850
	Medical Staffing Network	0.3	816
Life Sciences	Universal Health Services	3.3	21,200
	Amgen	1.8	10,100
	Techne Corporation	0.1	460
Consumer	Staples	11.6	29,912
	Outback Steakhouse	2.5	54,000
	Wild Oats	0.9	6,334
	Restoration Hardware	0.4	1,500

*Notes: Represents companies that had SBIC funding at some time in their history. Revenues and employee figures retrieved from MultexInvestor on March 19, 2003 using each company's last FY ending period.

In FY 2002 SBICs continued to finance across industries looking for solutions to cure cancer and other diseases, improve efficiencies, and enhance the quality of life. Below are just a few of the products and services currently being addressed by SBIC-backed companies by industry:

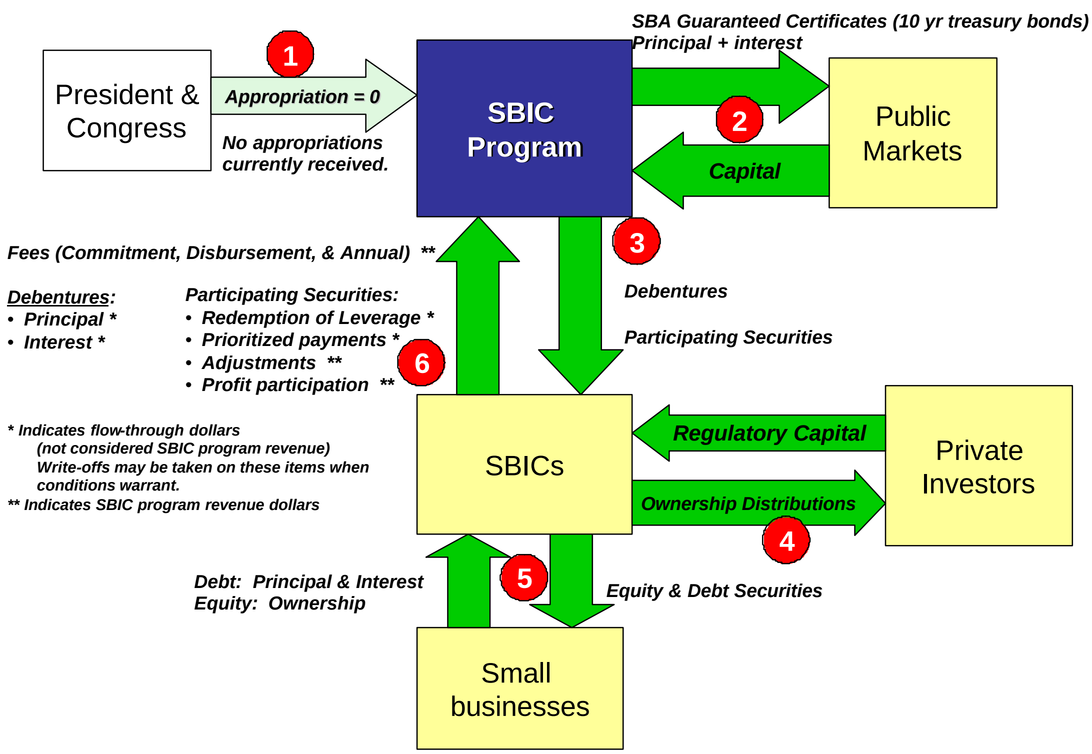
Industry	Company Name	State	Product/Service
Technology	Yipes Enterprises (formerly) PHX Communications Inc.	CA	Communications Services
	PPI/Time Zero Inc.	NJ	Electronic circuitry design, packaging, parts procurement and assembly expertise
	Aprilis Inc.	MA	Holographic data storage technology.
	Ibiquity Digital Corp.	MD	Communications Technology
	Trillion Digital Communications Inc.	AL	Digital Communications
	High Jump Software Inc.	MN	Supply chain execution software and services.
	Cryptek Inc.	VA	Computer/Network Security Solutions
Life Sciences	Algorx Pharmaceuticals Inc.	NJ	Pain management solutions
	Providence Service Corp.	AZ	Providence privatizes behavioral healthcare services for state administered programs through home-based and community-based counseling.
	Dynavax Technologies Corp.	CA	Treatments for allergy, inflammation-mediated diseases, infectious diseases and cancer
	Xcyte Therapies	WA	Therapeutic treatments for cancer and infectious disease.
	Southern Assisted Living Inc.	NC	Senior care services/facilities
	Memry Corp.	CT	Medical devices, including stents
Industrial/ Manufacturing	Neenah Foundry Company	WI	Municipal castings, including manhole frames, lids and grates, trench castings
	Thiel Cheese & Ingredients LLC	WI	Cheese Manufacturing
	Stylecraft	MS	Residential Electric Lighting Fixture Manufacturing
	Southern Weaving Company	SC	Narrow Fabric Mills
	Piedmont Hardwood Flooring LLC	GA	Cut Stock, Resawing Lumber, and Planing
Consumer Related	Alta Colleges Inc.	CO	Colleges, Universities, and Professional Schools
	Jenny Craig Inc.	CA	Diet and Weight Reducing Centers
	LaMadeleine Inc.	TX	French bakery and restaurant
	Aladdin Food Management Services Inc.	WV	Food Service Contractors
	Healthy Pet Corp.	CT	Veterinarian Services
Business & Financial Services	Tharpe Holding Company Inc.	NC	Supplier of full-choice recognition programs and products for service, retirement, sales, and safety occasions for employers.
	TRE Financial Services (aka Tax Refund Express)	TX	Electronic tax filing products and services to tax preparers, financial institutions, the small consumer loan industry, notaries, and insurance agents.
	Keystone Ranger Holdings Inc.	PA	Air Transportation services, including helicopter
	Cashland Inc.	OH	Financial Services
	CEI Holding Corp.	NY	Nonhazardous Waste Treatment and Disposal
	Bluefire Security Technologies	MD	Security technologies

4. SBIC Program Financial Statements

The SBIC program is in many respects a real business with identifiable revenues, expenses, assets, liabilities – and the financial risks that go along with them. We have therefore developed a set of financial statements for the program – a *preliminary* picture of the financial items driving SBIC program revenues, losses, and cash flow. (Disclaimer: These SBIC financial statements were prepared from the program office data for commercial presentation purposes and may differ from the figures presented in SBA's audited financial statements.)

SBIC Program Cash Flow. Exhibit 23 below provides a graphic overview of how money flows through the SBIC Program.

Exhibit 23 – SBIC Program Cash Flow



1. The SBIC program currently receives no congressional appropriation based on the zero subsidy cost estimated under the Federal Credit Reform Act. As necessary, SBA has the authority to borrow funds from the U.S. Treasury to pay for SBIC defaults and forced redemptions.
2. Based on authorization levels, commitment levels and draw approvals, SBA guarantees securities sold to the public markets to fund SBIC financings.
3. SBICs receive SBA leverage by issuing either a debenture or "participating security" (equity-type) investment.
4. Prior to receiving leverage, SBICs must have regulatory capital from private investors.
5. SBICs use the private capital and SBA leverage for financing small businesses in the form of either equity or debt securities.
6. Depending on the type of security issued by the SBIC, the SBICs make payments to the SBIC program as follows:
   - Debentures: principal and interest
   - Participating Securities: redemption of capital and contingent on profitability the following: prioritized payments, adjustments, and profit participation (payments may be in the form of cash or marketable securities)
   - Both: Commitment, Disbursement, and Annual Fees

Our analysis starts by charting the accounts of the SBIC program, so that they correspond appropriately with typical corporate financial statement items. The table below explains how this has been done using existing program data and new databases created out of all available statistics. Investment Division personnel costs and certain fees associated with the operating of the program (such as Examination Fees and Licensing Fees) are not included in these financial statements, due to the nature of government reporting of these items. Each of the items below is further explained later in this section within the financial notes and discussion.

Financial Statement Item	SBIC Program Item
Profit and Loss Statement	
• Revenues	Appropriations (Now at zero) SBIC Commitment, Disbursement, and Annual Charges SBIC Adjustment Payments Net Profit Participation (Profit Participation Payments Made To SBA + Gain (loss) on Sale of Securities Received)
• Expenses	Actual and projected losses from leverage invested into SBICs
• Net Income (loss)	Revenues minus Expenses
Balance Sheet	
• Assets	Cash Reserve Balance SBIC Investments • Active SBICs: o Outstanding leverage o Advanced prioritized payments o Loss Allocations in Active Portfolio • SBICs in Liquidations/Restructurings: o Gross amount transferred (leverage and advanced prioritized payments) plus additions post transfer (such as judgments) o Recoveries o Actual losses and projected losses from SBIC portfolio in Liquidations/Restructurings
• Liabilities & Capital	• Prioritized Payments Payable • Total Funding, including interim and guaranteed pooled securities (Note: This equals the amount of outstanding leverage in assets. As outstanding leverage is increased, because securities are pooled to the public, no cash outflow occurs, except from associated advanced prioritized payments. However, these securities represent a liability to the program, as the SBA is the guarantor.) • Cumulative SBIC Program Net Gains (Losses)

4.1 Consolidated SBIC Program Financials.

Since no financial statements have heretofore been developed and maintained for the SBIC program, a business starting point is required. Based on the beginning of the participating securities program, FY 1994 was chosen as the starting point, looking at only the debenture and participating security programs.

With the exception of appropriations and losses, all data was taken from the program records maintained by the Funding Administration Branch for the debenture and participating security programs for cohort years (FY of approvals) 1994 through 2002. These worksheets are developed by the Funding Administration Branch under the Office of Chief Administrative Officer. Appropriation data was provided by the Office of Chief Administrative Officer. Loss data was derived from the Subsidy Loss reports developed by Data Management under that same office. It should be noted that the SBIC financials disregard any leverage from previous cohort years and redeemable securities.

Like a company with different product lines, the SBIC program has two different types of securities: debentures and participating securities. As shown in the diagram above, both have different repayment terms and associated risks. Therefore, it is appropriate to separate out each "product" in order to analyze how each area is performing. Financial statements are provided below for each program, along with the "consolidated" SBIC program.

Profit and Loss Statement[27]

P&L for Cohort Years 1994 Through 2002 (in Millions of $)	FY 1994 Through 2002 Activity			
	Consolidated	Debenture	Participating Securities	Notes
REVENUE				
Appropriations	228.9	79.5	149.4	*a*
Commitment, Disbursement, and Annual Charge	247.5	84.9	162.6	*b*
SBIC Adjustment Payments	5.8	-	5.8	*c*
Profit Participation				
Profit Participation Payments Made To SBA	280.7	-	280.7	*d*
Gain (Loss) on In-kind Securities	(13.0)	-	(13.0)	*e*
Net Profit Participation	267.7	-	267.7	
TOTAL REVENUE	$ 749.9	$ 164.4	$ 585.5	
EXPENSE				
Actual Losses in Liquidations	(1.1)	(1.1)	-	*f*
Revenues minus Actual Losses	*748.8*	*163.3*	*585.5*	
Total Projected Losses on Assets	(384.6)	(88.2)	(296.4)	*g*
Consolidated Net Gain (Loss)	$ 364.2	$ 75.2	$ 289.1	

P&L Notes

a Appropriations are government subsidies used to offset losses in the program. Appropriations went to zero in FY 2000 for the debentures program and FY 2002 for the participating securities program. Information was provided by Data Management.

b Commitment, Disbursement, and Annual Charges are paid by the SBICs for the use of the capital.

c Adjustment Payments are paid per Part 107, Section 1520. The Investment Division assumes that adjustment payments are earned when received.

d Profit Participation payments are paid per Part 107, Section 1530. The Investment Division assumes that Profit Participation is earned when received by the Investment Division.

e Represents gains or losses from sales of in-kind securities received by the SBA.

f Losses represent actual write-offs/charge-offs on assets in liquidations.

g This represents the projected losses or loss allowance for all assets within the program both in the restructurings/liquidations portfolio and the active portfolio, as projected in the "Annual Summary of SBICs and Ultimate Loss Rate Projections Report." This number is estimated using historical information, as described in more detail in Section 4.2. However, as the Participating Securities Program has a ten year maturity, there is little historical data and the number above may be understated.

[27] These SBIC financial statements were prepared from the program office data for commercial presentation purposes and may differ from the figures presented in SBA's audited financial statements.

Balance Sheet[28]

Balance Sheet for Cohort Years 1994 through 2002 (in Millions of $)	End Of FY 2002			
	Consolidated	Debenture	Participating Securities	Notes
ASSETS				
Cash Reserve with zero beginning balance in 1994	54.3	93.9	(39.6)	a
SBIC Investments				
Active SBICs				
Outstanding Leverage	4,634.7	1,387.2	3,247.5	b
Unreimbursed Prioritized Payments	396.7	0.0	396.7	c
Cum Loss Allocations in Active Portfolio on Leverage/P	(238.3)	(65.9)	(172.4)	d
Net Active SBIC	4,793.2	1,321.3	3,471.8	
SBICs in Liquidation				
Leverage				
Gross Transferred Leverage	280.9	73.4	207.5	
Cum Recoveries	(3.1)	(2.9)	(0.3)	
Cum. Actual Losses	(1.1)	(1.1)	-	
Liquidation Portfolio Outstanding Leverage	276.7	69.4	207.2	e
Loss Allocation Total	(102.1)	(22.3)	(79.8)	f
Cum Total (Actual & Projected) Losses	(103.2)	(23.4)	(79.8)	
Net Liquidation SBIC Leverage	174.6	47.2	127.4	
Prioritized Payments				
Gross Unreimbursed Prioritized Payments Transferre	54.6		54.6	
Cum Recoveries	-		-	
Cum. Actual Losses	-		-	
Liquidation Outstanding Prioritized Payments	54.6		54.6	g
Cum Projected PP Losses	(44.3)		(44.3)	h
Net Liquidation Prioritized Payments	10.4		10.4	
Net SBICs in Liquidation	185.0	47.2	137.8	
TOTAL SBIC Investments	4,978.2	1,368.5	3,609.7	
TOTAL ASSETS	$ 5,032.5	$ 1,462.4	$ 3,570.1	
LIABILITIES AND CAPITAL				
Prioritized Payments Payable	33.5		33.5	i
Total Funding & Capital	4,634.7	1,387.2	3,247.5	j
Retained Earnings for Period	364.2	75.2	289.1	k
TOTAL LIABILITIES AND CAPITAL	$ 5,032.5	$ 1,462.4	$ 3,570.1	

Balance Sheet Notes

a Started with a $0 beginning balance and added in cashflows for the year from cashflow statement to derive ending balance.

b Outstanding investments to active participating security and debenture SBICs that are overseen by the Office of SBIC Operations. Investments in this area are fully funded by SBA-Guaranteed Securities and Interim Funding.

c This number reflects the amount of contingent unreimbursed prioritized payments that would be owed by the SBICs

[28] These SBIC financial statements were prepared from the program office data for commercial presentation purposes and may differ from the figures presented in SBA's audited financial statements.

Balance Sheet Notes

if they were profitable at FY 2002 end.

d This figure represents the loss allocations in the active portfolio, as calculated by the SBIC program loss measure, as published in the "Annual Summary of SBICs and Ultimate Loss Rate Projections Report". These figures differ from the cohort-based methodology required for budgeting under the Federal Credit Reform Act.

The calculation is based on an estimated Default Rate multiplied by an Estimated Loss Rate multiplied by the sum of the outstanding leverage and prioritized payments in the portfolio.

The estimated Default Rate is the total gross transferred leverage and advanced prioritized payments transferred into liquidation since 1966 divided by the total historical leverage plus advanced prioritized payment disbursements.

The Estimated Loss Rate is calculated by dividing the Allowances for Losses in Liquidation by the SBA Leverage When Transferred into Liquidation plus Advances Transferred to Liquidation. The Estimated Loss Rate applies only to those cases open in Liquidation.

Original SBIC and SSBIC calculations of both the default rate and the estimated loss rate are derived and applied separately.

As liquidations contains assets from preferred securities and debenture securities transferred to liquidations in years previous to FY 1994, a percentage of projected losses was derived based on the percentage of outstanding leverage attributable to FYs 1994 through 2002.

e Represents outstanding leverage of SBICs that have for regulatory or financial reasons been transferred to the Office of Liquidations. This number is gross transferred leverage minus collections minus losses plus any additions since post transfer such as judgments or loans. When transferred, outstanding leverage is purchased from pools by the SBA, causing a cash outflow.

f Represents projected losses in Liquidation Portfolio.

The Office of Liquidations performs an estimate of all projected net recoveries for all outstanding leverage that has been transferred to its office at the end of each FY. The assets of an SBIC from which SBA will seek to recover the leverage may include outstanding equities, debt securities, notes, or tangible property as well as any investment instrument an SBIC might have utilized in providing financing. At that time, using a detailed bottoms-up approach, on an asset by asset basis, the office reviews the recoverable value of the asset based on valuations, estimates, and appraisals as well as payment history, security, and other pertinent and available information dependent upon the type of holding, the priority of the investment, and the overall market conditions. The Office reassesses this estimate each year.

As liquidations contain assets from preferred securities and debenture securities transferred to liquidations in years previous to FY 1994, a percentage of projected losses was derived based on the percentage of outstanding leverage in liquidations attributable to FYs 1994 through 2002.

g The number shown here is the total of outstanding prioritized payments transferred minus any recoveries or actual losses. Because Prioritized Payments are a contingent liability payable only from profits of the SBIC, they present a greater risk than outstanding leverage. Therefore, they are separated on the balance sheet from outstanding leverage to indicate this higher risk.

Balance Sheet Notes

While recoveries are ascertained from the Funding Administration Branch worksheets, actual losses for debentures are derived based on the percentage of recoveries attributable to cohort FYs 1994 through 2002 (i.e., it is assumed that recovery percentages of cohort years to overall recovery equals the actual loss percentage of cohort years to overall actual losses for that FY.)

h Represents projected losses of prioritized payments. (See note f above to see how this is estimated.)
As shown, about 80% of prioritized payments transferred to liquidations are estimated as being a loss because of their contingent nature. These figures differ from the cohort-based methodology required for budgeting under the Federal Credit Reform Act.

i This indicates the amount of Prioritized Payments, payable by the SBA as guarantor on behalf of the Active Participating Securities that do not have profits with which to make the payments.

j Funding in terms of Interim Funding and Guaranteed Pools for Participating Securities and Debentures. Not included are commitments that have not yet been drawn down of $3,668.1 million. They are not included in the balance sheet because they are contingent upon both a draw-down request and SBA approval.

k This number is derived based on an initial zero cash balance for 1994 plus retained net income (losses) for each year.

4.2 Financial Discussion

Profit and Loss (P&L) Statement

While the SBIC program is not designed to make a profit, it is SBA's intention to ensure that the program – over time – does not lose money either, given appropriations and subsidies. The Profit & Loss Statement, including both actual and projected losses, should help indicate whether the program will break even with its current portfolio of investments.

As shown by the P&L Statement, between FY 1994 and 2002, the Debenture Program incurred a net gain of $75.2 million and the Participating Securities Program incurred a net gain of $289.1 million, resulting in a total $364.2 million net gain. However, as the Participating Securities program has not yet completed a full business cycle, with ten year terms for guaranteed securities, projected losses must be looked at with some reservation. (Appendix B provides a full description of how projected losses are derived per the "Annual Summary of SBICs and Ultimate Loss Rate Projections," produced by Data Management.) We anticipate that as a fund of venture capital funds, the SBIC program's results will continue to reflect that of the rest of venture capital and the market.

Balance Sheet

While the Participating Securities Program appears to outperform the Debentures Program based on the P&L, the Balance Sheet demonstrates that, based on cash, the Debenture Program performs better. As shown, assuming a cash $0 beginning balance for each program, at the end of FY 2002, the debenture program carried a $93.9 million cash reserve, while the participating securities program carried a negative $39.6 million cash balance, for a combined program cash balance total of $54.3 million. Reasons for this difference include:

- Participating Security transfers into Liquidations of $207.5 million of leverage (although $.3 million was recovered) and $54.6 million in prioritized payments through FYs 2000 and 2002. Transfers into Liquidations cause an immediate cash outflow for the program.

- Prioritized payments are advanced to trust certificate holders by the SBA, creating a receivable. As with any receivable, as it goes up, cash balance goes down. By the end of FY 2002, prioritized payments owed by the SBICs in the active portfolio totaled $396.7 million. While the offsetting $33.5 million in prioritized payments payable under liabilities somewhat offsets this figure, it still leaves over $363.2 million as a cash out, not counting the additional $54.6 million in Liquidations. Exhibit 24 on the next page shows the net prioritized payments in the active portfolio accumulating over time. As shown, additional prioritized payments resulted in cash out of $129.2 million in the active portfolio in FY 2002.

Cash Drivers – Program Inflows and Outflows

The primary sources of outflows for the Debenture and Participating Securities Program are Advanced Prioritized Payments made on behalf of the SBICs and Transfers to Liquidations.[29] The primary cash inflows are Revenues, Recoveries in Liquidations, and Appropriations. (Prior to FY 2002, the SBIC program received appropriations to cover expected program costs.) For the program to operate in a cost neutral manner, fees and other inflows must be enough to cover losses sustained by the program over time. Timing is a relevant factor for measuring results. Generally, fees tend to come early in the loan guarantee cycle, while transfers to liquidations (also known as "defaults") will vary, depending on market conditions, as will recoveries. As discussed in Section 2.2, when the market is high, SBIC

[29] Neither actual nor projected losses impact the cash reserve as projected losses are accounted for in the balance sheet (offsetting P&L losses) and actual losses occur in liquidations where cash associated with the asset was already paid out.

venture funds (as with the average venture fund) tend to perform well. When the market is down, it takes longer to realize returns. Therefore, to assess the financial performance of the SBIC program, SBA must estimate the percentage of outstanding guarantees that are likely to default as well as estimate the likely recoveries on any SBICs moved into liquidation status.[30]

Cash drivers are identified below by year from FY 1994 through 2002, in order to begin evaluating trends.

Exhibit 24 – SBIC Cash Drivers ($Millions)

CASH DRIVERS (In $Millions)	FY 1994	FY 1995	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	Totals	Notes
Cash Inflows											
Other Revenues	1.3	5.1	11.2	24.5	50.9	65.9	149.0	139.2	73.8	521.1	
Appropriations	33.7	42.0	40.5	21.7	20.2	20.3	24.3	26.2	-	228.9	
Recoveries	-	-	-	-	-	-	0.2	-	2.9	3.1	
Cash Outflows											
Net Transfers to Liquidations	-	-	-	-	-	(0.8)	(11.6)	(76.5)	(246.7)	(335.5)	a
Net Prioritized Payments	-	(3.2)	(15.8)	(26.4)	(31.0)	(40.3)	(29.6)	(87.7)	(129.2)	(363.2)	b
Cashflow	35.0	43.9	35.9	19.8	40.1	45.1	132.4	1.3	(299.3)	54.3	
Cash Beginning	-	35.0	78.9	114.8	134.6	174.7	219.8	352.2	353.5		
Cash Ending	35.0	78.9	114.8	134.6	174.7	219.8	352.2	353.5	54.3		

Notes: a) Net transfers to liquidations includes transfers to liquidations, any post transfer additions, such as judgements, minus any transfers back to operations & redeemable securities transferred. (Includes both leverage and prioritized payments.)

b) Net prioritized payments are all prioritized payments that are owed by the SBICs that have actually been paid out by the SBIC program not transferred to liquidations.

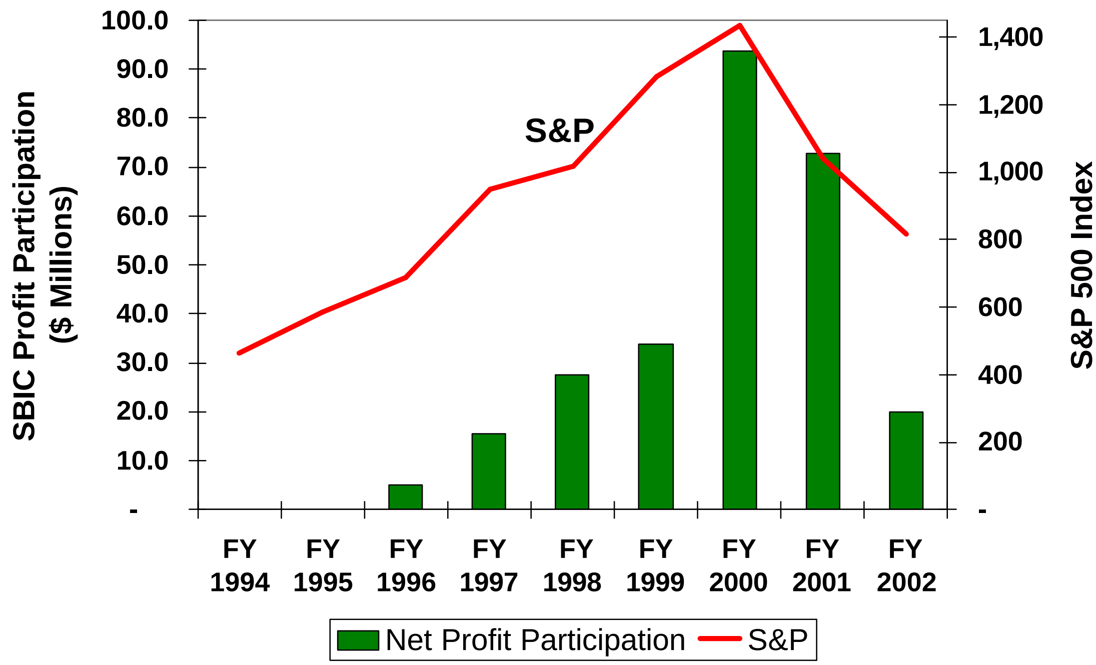
As shown, since FY 2000 (the height of the venture capital market), revenues went down considerably and recoveries were negligible, while transfers to Liquidations and Prioritized Payments went up. Because of these conditions, cash decreased by 85% in FY 2002. Cash went from a balance of $353.5 million in FY 2000 to a balance of $54.3 million in FY 2002.

Given the decline in the stock market since FY 2000 and the resulting impacts to the venture industry, this is to be expected. Across the years the program returned $521.1 million in revenues to the U.S. Treasury. However, as discussed in Section 2.2, when the stock market is down, the venture capital market suffers. As shown in Exhibit 25, when the market was high, SBICs returned profit participation, which has decreased since FY 2000. We anticipate that SBICs will continue to perform similarly to the rest of the venture capital industry.

Since the program is designed to break even over time, the SBA continues to assess and analyze the structure of the program in terms of fees and profit participation to keep the program at zero appropriation. Given the vicissitudes of the market, the fees and profit participation need to be high enough to cover cash outflows during the lows in the economic cycle. In addition, the SBA has developed and is currently testing a risk assessment model designed to provide increased communications and scrutiny commensurate with the assessed risk.

[30] For budgeting and accounting purposes, the SBIC program is included under the Federal Credit Reform Act (FCRA). The FCRA requires Federal credit agencies to estimate the net present value of the cost of loans and loan guarantees on a cohort basis and receive any required appropriations prior to entering into loan or loan guarantee commitments. To the extent that the original cost estimates underestimate the actual cost, permanent indefinite budget authority is available to cover the cost. To the extent that the original cost estimate overestimated the actual cost, the excess reserve amount is returned to Treasury and is not available to the program for any purpose without additional appropriations action

Exhibit 25 – Participating Security SBIC Net Profit Participation versus S&P Index[31]



[31] S&P Data derived from Commodity Systems Incorporated via Yahoo.com, using September historical prices (symbol SPB) through December 31, 2002.

5. SBIC Licensee Financials

Since the SBIC program's financial health is driven by how actual SBIC licensees are performing, this section pertains to SBIC licensee funds. In this preliminary analysis, it has not been possible, due to insufficient data and reporting, to use "industry standard" performance measurements for a typical venture fund, including Internal Rate of Return (IRR) and Realization Ratios (Distributions to Paid-in-Capital Ratio, Residual Value to Paid-In-Capital Ratio, and Total Value to Paid-In-Capital). The SBIC Program is considering measuring or having SBICs report these measurements to the SBA. This will help the program better understand how SBICs perform against comparable non-SBIC funds.

In any event, while performance compared to the rest of the venture capital industry is important, the SBIC Program's primary interest is in ensuring that SBICs will be able to repay their leverage and prioritized payments. Therefore, the SBIC Program analyzes its funds' ability to repay in part by using a measurement called "Capital Impairment," as calculated in the SBIC regulations (13 CFR 107.1840). To simplify this calculation, Capital Impairment of 100% means that the private investors may lose their entire capital, exposing the Government to loss. This holds true for the principal amounts of debentures and participating securities guaranteed by the Government. In the case of participating securities, there is a further risk of loss related to the advanced prioritized payments. A participating securities licensee is only obligated to reimburse the Government for advanced prioritized payments if it earns a profit.

Because of the cyclical nature of venture capital, the "J-curve" effect, and the fact that many venture investments typically suffer total or partial losses, the Investment Division recognizes that Capital Impairment alone provides an incomplete picture of a fund's ability to repay SBA leverage and prioritized payments. As such, the Investment Division recently created a Risk Management Branch under the Office of Operations to revisit SBA Valuation Guidelines and develop a new risk model.

5.1 Consolidated Licensee Financials

By looking at the combined financials of SBIC Licensees, it is possible to develop an understanding of:

- Profits and losses of SBIC Licensees;
- Assets underlying the SBIC Program;
- How the program has grown or contracted; and
- Percentage of SBA leverage to Private Capital and overall Capital base.

The combined financials for active SBICs by fiscal year since FY 1994 appear on the following pages. Because bank-owned SBICs, which typically do not make use of SBA leverage, comprise such a large share of the aggregate private capital and look much different than other SBICs in terms of profits, losses, assets, liabilities, and capital, they have been separated into their own category. (Note: SBICs in liquidations are included in financials up through the FY in which they are transferred.)

Exhibit 26 – Consolidated SBIC Licensee Financials by Fiscal Year[32]

	1994	1995	1996	1997	1998	1999	2000	2001	2002
Number of Active SBICs	237	254	261	264	280	292	321	367	383
Bank	59	58	58	63	68	69	75	77	79
Debenture	102	106	104	96	96	98	103	110	115
Specialized	76	69	68	67	63	60	50	46	33
Participating	0	21	31	38	53	65	93	134	156

Income Statement

INCOME STATEMENT (In Millions of $)	1994	1995	1996	1997	1998	1999	2000	2001	2002	Total
INVESTMENT INCOME										
Interest & Dividends	185.6	198.7	257.1	215.0	310.0	298.4	337.3	341.4	369.5	2,513.1
Income (Loss) from Investments in Partnerships/ Flow-through Entities or Section 301D Licensees	0.4	9.6	8.3	52.9	68.8	35.1	7.6	4.6	6.6	193.9
Fees	7.8	9.4	16.5	13.9	19.3	21.0	24.9	22.5	21.4	156.7
Other Income	53.8	63.9	79.9	75.4	123.9	97.1	113.3	239.4	190.9	1,037.6
GROSS INVESTMENT INCOME	247.6	281.7	361.8	357.3	522.0	451.5	483.1	607.8	588.4	3,901.3
EXPENSES										
Interest Expense	62.8	66.5	71.8	74.1	93.6	114.4	126.3	219.4	278.5	1,107.4
Officers & Employee Compensation and Benefits	26.6	32.8	40.5	44.0	55.8	82.0	100.8	56.3	31.5	470.2
Investment Advisory and Management Services	43.9	48.9	54.9	69.0	109.4	129.2	199.3	323.5	311.9	1,290.1
Other Expenses	86.7	80.1	53.3	51.0	87.9	87.6	61.9	198.9	137.3	844.7
TOTAL EXPENSES	220.1	228.2	220.5	238.0	346.7	413.2	488.3	798.1	759.2	3,712.3
NET INVESTMENT INCOME (LOSS) BEFORE TAXES	27.6	46.8	132.0	119.2	175.4	38.3	(5.2)	(190.3)	(170.9)	173.1
NET REALIZED GAIN (LOSS) ON INVESTMENTS BEFORE INCOME TAXES (1)	456.8	371.6	734.7	936.1	1,235.1	920.2	3,779.1	6,076.8	1,026.2	15,536.7
NET INCOME (LOSS) BEFORE TAXES & NONRECURRING	363.2	327.1	705.6	566.2	873.5	446.5	1,458.0	1,977.9	749.4	7,467.4
Income Tax Expense	139.4	76.3	239.3	196.9	293.5	151.7	476.7	578.1	258.3	2,410.3
NET INCOME (LOSS) BEFORE NONRECURRING ITEMS	507.1	346.2	640.8	877.1	1,109.8	826.5	3,319.8	5,341.9	601.1	13,570.3
Nonrecurring Items	18.3	25.5	13.9	31.1	(16.4)	10.2	28.2	(25.7)	(0.9)	84.1
NET INCOME (LOSS)	487.3	318.5	628.1	850.2	1,113.4	793.9	3,287.0	5,316.4	600.2	13,395.1

Consolidated SBIC Licensee Balance Sheet

Consolidated Balance Sheet (Millions of $)	1994	1995	1996	1997	1998	1999	2000	2001	2002
ASSETS									
Total Current Assets	1,710.9	1,722.0	2,147.0	1,871.3	2,590.0	1,899.8	3,129.5	3,898.1	6,332.2
Loans and Investments									
Portfolio Securities									
Loans Net Value	769.3	767.6	766.5	635.2	614.2	762.1	778.3	863.9	744.5
Debt Securities Net Value	547.7	730.7	925.7	1,092.7	1,453.2	1,486.8	1,943.4	1,956.5	2,201.1
Equity Securities Net Value	3,120.9	3,340.4	4,159.1	4,172.2	7,075.8	7,110.9	19,487.0	14,824.7	11,550.2
Total Portfolio Value	4,437.8	4,838.7	5,851.3	5,900.2	9,143.2	9,358.3	22,199.0	17,645.1	14,495.8
Total Assets Acquired Value	30.6	32.0	33.1	25.0	24.7	24.0	19.0	11.5	10.3
Total Loans & Investments at Cost	*3,523.5*	*4,178.1*	*4,778.4*	*5,294.4*	*7,325.1*	*8,644.4*	*13,554.8*	*13,395.8*	*14,169.8*
Total Loans & Investments at Value	4,653.4	5,116.7	6,136.6	6,040.6	9,319.6	9,819.3	22,805.7	17,879.2	14,874.8
Loans & Investments Net Current Maturities	4,498.5	4,987.1	5,980.6	5,900.2	9,206.2	9,700.4	22,677.9	17,717.9	14,736.5
Other Investment Asset	5.7	1.9	2.0	2.1	2.4	2.5	-	-	-
Total Other Assets	39.4	115.3	109.9	142.9	159.5	179.5	181.5	240.3	427.9
TOTAL ASSETS	6,263.4	6,826.3	8,239.6	7,916.5	11,949.4	11,784.4	25,996.3	21,856.3	21,496.6
LIABILITIES AND CAPITAL									
Liabilities									
Current Liabilities	682.1	499.6	644.0	858.3	1,023.0	1,351.1	2,109.1	2,922.3	3,292.6
Other Liabilities	386.8	450.6	496.0	155.1	655.2	167.5	1,108.1	1,067.6	626.1
Long-Term Debt									
SBA Notes and Debentures Payables	533.4	574.7	637.6	683.7	760.9	808.0	818.0	933.3	1,231.6
Other Notes and Debentures Payable	124.8	126.7	173.9	194.4	242.6	363.0	436.4	660.7	1,725.0
Total Long-Term Debt	658.2	701.4	811.4	878.2	1,003.5	1,170.9	1,254.4	1,594.0	2,956.7
Total Liabilities	1,747.7	1,651.6	1,951.4	1,891.6	2,681.6	2,689.5	4,471.7	5,583.9	6,875.3
Total SBA Redeemable Securities	0.5	52.9	314.7	600.6	794.7	943.2	1,545.2	2,114.6	2,697.7
Total Private Contributed Capital	2,798.6	3,452.0	3,830.5	3,810.8	5,129.0	5,973.1	9,208.9	7,326.6	9,037.3
3% SBA Preferred Stock Purchased by SBA	137.6	94.6	58.6	46.0	34.3	28.5	24.2	19.6	10.8
Other Capital Adjustments	-	-	-	-	-	(0.3)	(7.9)	(17.8)	(19.1)
Unrealized Gain (Loss) on Securities held	761.3	716.6	942.1	595.5	1,299.4	947.1	8,095.7	3,425.5	311.2
Undistributed Realized Earnings	816.1	831.4	1,092.0	913.6	1,913.8	1,069.1	2,607.6	3,350.5	2,539.6
TOTAL LIABILITIES AND CAPITAL	6,263.4	6,826.3	8,239.6	7,917.2	11,958.4	11,784.3	25,996.3	21,856.3	21,496.6

Note: "Total Loans and Investment Values" include any unrealized gains and losses as well as any depreciation. By comparing the "Total Loans and Investments at Cost" versus "Total Loans and Investments at Value" one can identify the net changes. Exhibit 32 later in this document under the analysis section provides this analysis.

[32] The data reflects the annual 468s received in each FY for SBICs still active by the end of each FY. It does not include any SBICs that were transferred to Liquidations or surrendered licenses prior to the end of the FY.

Exhibit 27 – Consolidated Debenture and SSBIC Financials by Fiscal Year[33]

Income Statement

	1994	1995	1996	1997	1998	1999	2000	2001	2002	Total
Number of Active SBICs	178	174	172	163	158	158	153	155	148	
(In Millions of $)										
INVESTMENT INCOME										
Interest & Dividends	92.9	103.0	117.2	109.1	123.9	156.8	151.6	163.1	186.5	1,203.8
Income (Loss) from Investments in Partnerships/ Flow-through Entities or Section 301D Licensees	0.6	1.0	1.4	0.4	1.6	1.2	1.6	2.4	3.5	13.7
Fees	3.2	4.3	8.0	4.8	6.9	10.2	9.0	8.6	7.4	62.4
Other Income	13.5	13.8	17.7	19.1	23.4	21.8	20.4	20.4	14.3	164.4
GROSS INVESTMENT INCOME	110.1	122.0	144.3	133.4	155.8	190.0	182.6	194.4	211.7	1,444.3
EXPENSES										
Interest Expense	50.3	54.7	58.2	54.0	61.4	74.4	74.1	88.9	99.1	615.0
Officers & Employee Compensation and Benefits	13.4	12.1	13.8	13.2	15.2	18.0	15.7	14.1	11.7	127.3
Investment Advisory and Management Services	12.0	15.0	19.9	20.8	23.2	28.1	37.1	47.8	55.7	259.7
Other Expenses	25.4	20.4	23.1	23.0	25.5	29.8	31.6	36.7	43.8	259.2
TOTAL EXPENSES	101.1	102.1	115.0	110.9	125.3	150.3	158.6	187.5	210.3	1,261.2
NET INVESTMENT INCOME (LOSS) BEFORE TAXES	9.0	19.9	29.4	22.5	30.5	39.7	23.9	6.9	1.4	183.1
NET REALIZED GAIN (LOSS) ON INVESTMENTS BEFORE INCOME TAXES (1)	8.0	8.8	50.4	49.5	120.2	33.5	161.1	72.9	(75.7)	428.6
NET INCOME (LOSS) BEFORE TAXES & NONRECURRING	18.8	28.6	58.6	46.3	116.2	55.1	121.5	60.3	5.2	510.5
Income Tax Expense	5.7	1.7	8.3	4.4	24.8	5.2	11.1	12.7	3.9	77.9
NET INCOME (LOSS) BEFORE NONRECURRING ITEMS	13.0	26.9	71.4	67.5	125.8	68.0	173.9	67.2	(78.2)	535.6
Nonrecurring Items	0.8	(0.5)	0.8	1.6	(8.4)	(16.8)	(1.4)	(8.2)	(1.0)	(33.2)
NET INCOME (LOSS)	13.0	26.3	71.3	69.3	121.0	51.1	172.5	59.0	(79.3)	504.2

Balance Sheet

Debentures, SSBICs (In Millions of $)	1994	1995	1996	1997	1998	1999	2000	2001	2002
Total Active Funds Reported at end of FY	178	175	172	163	159	158	153	156	148
ASSETS									
Total Current Assets	506.4	448.1	499.0	561.7	530.1	516.9	543.2	498.6	474.8
Total Loans and Investment at Cost	*1,130.6*	*1,247.8*	*1,411.2*	*1,414.1*	*1,615.9*	*1,878.0*	*2,057.8*	*2,250.5*	*2,394.6*
Total Loans and Investment Value	1,289.4	1,430.2	1,604.1	1,611.9	1,862.2	2,078.1	2,520.6	2,616.6	2,540.0
Loans and Investments Net of Current Maturities	1,159.7	1,317.8	1,499.2	1,511.7	1,786.4	1,976.0	2,411.8	2,501.7	2,422.0
Other Investment Asset	5.7	1.9	2.0	2.1	2.4	2.5	-	-	-
Total Other Assets	14.2	15.5	20.8	20.3	27.8	27.6	36.3	40.7	43.3
TOTAL ASSETS	1,694.8	1,783.3	2,021.0	2,095.8	2,346.9	2,523.1	2,991.3	3,041.0	2,940.1
LIABILITIES AND CAPITAL									
Liabilities									
Current Liabilities	235.2	166.6	166.7	244.9	191.7	253.9	339.5	257.7	120.6
Other Liabilities	67.7	51.4	62.5	46.3	69.7	48.5	73.8	57.3	36.6
Long-Term Debt									
SBA Notes and Debentures Payables	495.2	553.2	619.6	660.2	737.4	785.2	792.4	892.8	1,166.1
Other Notes and Debentures Payable	98.0	82.9	105.6	38.7	74.8	107.4	166.2	248.9	197.4
Total Long-Term Debt	593.2	636.1	725.2	698.9	812.2	892.6	958.5	1,141.7	1,363.5
Total Liabilities	884.8	854.1	954.3	990.1	1,073.6	1,195.0	1,371.8	1,456.7	1,520.6
Redeemable Securities									
4% Redeemable Preferred Securities									
Outstanding	0.5	42.6	54.9	54.5	53.5	51.1	46.4	40.6	39.6
Cumulative Unpaid 4% Distribution	-	3.1	4.6	8.0	9.3	8.3	7.7	7.1	7.7
Total 4% Redeemable Preferred	0.5	45.8	59.5	62.4	62.8	59.4	54.1	47.7	47.4
Total SBA Redeemable Securities	0.5	45.8	59.5	62.4	62.8	59.4	54.1	47.7	47.4
Total Private Contributed Capital	559.5	625.0	737.4	779.4	890.1	1,016.3	1,056.3	1,160.5	1,345.8
3% SBA Preferred Stock Purchased by SBA	137.6	94.6	58.6	46.0	34.3	28.5	24.2	19.6	10.8
Other Capital Adjustments	-	-	-	-	-	(0.3)	(2.3)	(1.9)	(2.6)
Unrealized Gain (Loss) on Securities held	119.5	135.0	140.8	137.3	171.3	162.4	391.5	301.0	97.8
Undistributed Realized Earnings	(8.7)	1.7	20.0	22.2	56.6	1.0	44.6	4.1	(123.5)
TOTAL LIABILITIES AND CAPITAL	1,694.8	1,783.3	2,021.0	2,096.5	2,346.9	2,523.0	2,991.3	3,041.0	2,940.1

[33] The data reflects the annual 468s received in each FY for SBICs still active by the end of each FY. It does not include any SBICs that were transferred to Liquidations or surrendered licenses prior to the end of the FY.

Exhibit 28 – Consolidated Bank-Owned SBIC Financials by Fiscal Year[34]

Income Statement

	1994	1995	1996	1997	1998	1999	2000	2001	2002	Total
Number of Active SBICs	59	58	58	63	68	69	75	77	78	
(In Millions of $)										
INVESTMENT INCOME										
Interest & Dividends	92.8	97.0	140.0	95.7	169.8	125.3	143.1	144.7	146.9	1,155.3
Income (Loss) from Investments in Partnerships/ Flow-through Entities or Section 301D Licensees	(0.2)	8.5	6.5	52.6	69.2	31.2	2.6	0.6	1.3	172.4
Fees	4.7	4.7	3.9	7.6	11.2	9.8	14.4	11.5	10.3	78.0
Other Income	40.3	49.0	64.2	46.1	87.7	65.1	84.1	204.2	165.1	805.7
GROSS INVESTMENT INCOME	137.5	159.2	214.7	201.9	337.9	231.5	244.1	361.0	323.6	2,211.5
EXPENSES										
Interest Expense	12.5	11.8	13.3	19.4	31.4	37.7	50.2	127.0	173.2	476.5
Officers & Employee Compensation and Benefits	13.2	15.2	12.7	30.8	40.6	64.0	85.0	42.1	19.7	323.4
Investment Advisory and Management Services	31.9	33.2	33.7	25.4	53.2	51.4	77.5	125.2	57.1	488.6
Other Expenses	61.3	65.1	43.4	22.0	53.6	43.9	11.0	131.5	55.7	487.4
TOTAL EXPENSES	118.9	125.3	103.1	97.5	178.7	196.9	223.8	425.8	305.6	1,775.9
NET INVESTMENT INCOME (LOSS) BEFORE TAXES	18.6	33.9	111.6	104.4	159.2	34.5	20.4	(64.8)	18.0	435.6
NET REALIZED GAIN (LOSS) ON INVESTMENTS BEFORE INCOME TAXES (1)	448.9	362.9	684.4	860.7	1,071.2	719.4	2,711.6	4,131.6	1,145.1	12,135.8
NET INCOME (LOSS) BEFORE TAXES & NONRECURRING	344.4	299.0	647.0	520.0	757.3	391.5	1,336.5	1,917.6	744.2	6,957.5
Income Tax Expense	133.7	80.9	230.9	192.5	268.7	146.5	465.6	565.4	254.4	2,338.6
NET INCOME (LOSS) BEFORE NONRECURRING ITEMS	494.1	319.8	570.1	791.3	954.6	627.2	2,288.9	3,534.8	912.8	10,493.7
Nonrecurring Items	17.5	26.0	13.2	29.1	(8.2)	27.3	30.4	(16.9)	-	118.4
NET INCOME (LOSS)	474.4	292.8	557.6	762.3	962.8	611.6	2,258.4	3,518.2	912.8	10,350.8

Balance Sheet

Banks (In Millions of $)	1994	1995	1996	1997	1998	1999	2000	2001	2002
Active Funds Reported at end of FY	59	58	58	63	68	69	75	77	79
ASSETS									
Total Current Assets	1,204.5	1,231.8	1,461.7	1,039.9	1,755.3	1,149.5	2,200.0	2,982.9	5,461.6
Loans and Investments									
Portfolio Securities									
Loans Net Value	175.8	184.5	156.5	135.3	143.8	89.9	74.1	116.9	77.0
Debt Securities Net Value	358.0	421.4	432.4	476.8	655.8	656.4	962.8	914.3	862.6
Equity Securities	2,708.4	2,812.7	3,429.2	3,048.0	5,505.8	5,098.0	13,909.0	9,485.9	7,177.4
Total Portfolio Value	3,242.3	3,418.6	4,018.2	3,660.1	6,305.4	5,842.8	14,936.2	10,517.2	8,117.0
Total Assets Acquired Value	1.9	3.4	1.0	0.2	2.2	0.0	0.0	0.0	0.9
Total Loans and Investment at Cost	*2,392.8*	*2,861.6*	*3,122.4*	*3,291.1*	*4,811.7*	*5,495.9*	*9,279.6*	*7,735.1*	*7,884.7*
Total Loans and Investment Value	3,364.0	3,609.3	4,251.7	3,758.3	6,431.9	6,238.7	15,475.9	10,700.7	8,442.0
Loans and Investments Net of Current Maturities	3,338.8	3,592.3	4,200.8	3,718.3	6,395.1	6,225.2	15,462.7	10,659.7	8,426.9
Total Other Assets	25.2	96.1	79.5	106.4	112.1	128.1	111.6	137.3	311.7
TOTAL ASSETS	4,568.6	4,920.3	5,742.0	4,864.6	8,253.7	7,504.9	17,781.7	13,779.9	14,200.2
LIABILITIES AND CAPITAL									
Liabilities									
Current Liabilities	446.9	327.1	475.1	611.7	826.8	1,071.8	1,747.8	2,615.1	3,109.7
Other Liabilities	319.1	399.2	432.5	108.1	585.4	118.9	1,029.6	989.8	566.2
Long-Term Debt									
SBA Notes and Debentures Payables	38.2	12.5	9.0	12.5	12.5	15.5	15.5	18.7	31.7
Other Notes and Debentures Payable	26.8	39.1	68.2	155.7	167.8	255.6	270.2	411.8	1,527.6
Total Long-Term Debt	65.0	51.6	77.2	168.2	180.3	271.1	285.7	430.5	1,559.3
Total Liabilities	862.8	777.8	984.9	888.0	1,592.5	1,461.7	3,063.1	4,035.5	5,235.2
Total 4% Redeemable Preferred	-	1.1	1.2	1.2	1.2	1.3	1.3	1.4	1.4
Total Private Contributed Capital	2,239.2	2,728.2	2,894.9	2,688.1	3,735.2	4,285.2	7,041.0	4,372.2	5,599.4
3% SBA Preferred Stock Purchased by SBA	-	-	-	-	-	-	-	-	-
Other Capital Adjustments	-	-	-	-	-	-	-	-	0.2
Unrealized Gain (Loss) on Securities held	641.8	573.0	766.1	377.0	997.7	552.9	5,112.4	1,972.2	210.1
Undistributed Realized Earnings	824.8	840.1	1,094.9	910.3	1,886.9	1,127.5	2,564.0	3,398.7	3,153.9
Total Liabilities, Redeemable Securities and Partners' Capital	4,568.6	4,920.3	5,742.0	4,864.6	8,262.7	7,504.9	17,781.7	13,779.9	14,200.2

[34] The data reflects the annual 468s received in each FY for SBICs still active by the end of each FY. It does not include any SBICs that were transferred to Liquidations or surrendered licenses prior to the end of the FY.

Exhibit 29 – Consolidated Participating Security Financials by Fiscal Year[35]

Income Statement

	1994	1995	1996	1997	1998	1999	2000	2001	2002	Total
Number of Active SBICs	0	21	31	38	53	65	93	134	156	
(In Millions of $)										
INVESTMENT INCOME										
Interest & Dividends	-	(1.3)	(0.1)	10.2	16.3	16.3	42.6	33.6	36.1	153.9
Income (Loss) from Investments in Partnerships/ Flow-through Entities or Section 301D Licensees	-	0.1	0.3	(0.0)	(2.1)	2.7	3.5	1.6	1.8	7.8
Fees	-	0.5	4.5	1.5	1.2	1.0	1.5	2.4	3.7	16.3
Other Income	-	1.2	(2.0)	10.3	12.9	10.1	8.9	14.8	11.5	67.5
GROSS INVESTMENT INCOME	-	0.5	2.8	22.0	28.3	30.1	56.5	52.4	53.1	245.5
EXPENSES										
Interest Expense	-	0.0	0.3	0.8	0.9	2.3	2.0	3.4	6.3	15.9
Officers & Employee Compensation and Benefits	-	5.5	13.9	-	-	-	-	0.1	-	19.5
Investment Advisory and Management Services	-	0.7	1.4	22.8	33.0	49.8	84.6	150.4	199.1	541.8
Other Expenses	-	(5.4)	(13.2)	6.1	8.7	13.9	19.3	30.8	37.9	98.1
TOTAL EXPENSES	-	0.8	2.4	29.6	42.6	66.0	105.9	184.8	243.3	675.3
NET INVESTMENT INCOME (LOSS) BEFORE TAXES	-	(6.9)	(8.9)	(7.6)	(14.3)	(35.9)	(49.5)	(132.4)	(190.2)	(429.8)
NET REALIZED GAIN (LOSS) ON INVESTMENTS BEFORE INCOME TAXES (1)	-	-	-	25.9	43.7	167.3	906.4	1,872.3	(43.2)	2,972.3
NET INCOME (LOSS) BEFORE TAXES & NONRECURRING	-	(0.6)	-	-	-	-	-	-	-	(0.6)
Income Tax Expense	-	(6.3)	-	-	-	-	-	-	-	(6.3)
NET INCOME (LOSS) BEFORE NONRECURRING ITEMS	-	(0.6)	(0.8)	18.3	29.4	131.4	856.9	1,739.9	(233.4)	2,541.1
Nonrecurring Items	-	0.0	0.0	0.3	0.2	(0.2)	(0.8)	(0.6)	0.1	(1.1)
NET INCOME (LOSS)	-	(0.6)	(0.8)	18.6	29.6	131.2	856.1	1,739.3	(233.4)	2,540.0

Balance Sheet

Participating Securities (In Millions of $)	1994	1995	1996	1997	1998	1999	2000	2001	2002
Active Funds Reported at end of FY	-	21.0	31.0	38.0	53.0	65.0	93.0	134.0	156.0
ASSETS									
Total Current Assets	-	42.1	186.3	269.7	304.6	233.5	386.3	416.6	395.8
Loans and Investments									
Portfolio Securities									
Loans Net Value	-	2.2	11.0	24.2	23.3	35.2	48.4	50.7	55.0
Debt Securities Net Value	-	6.4	47.6	103.6	147.7	153.9	253.9	308.5	348.2
Equity Securities Net Value	-	68.6	222.3	541.1	853.3	1,306.7	4,482.9	4,197.0	3,468.8
Total Portfolio Value	-	77.2	280.9	668.8	1,024.2	1,495.7	4,785.2	4,556.2	3,871.9
Total Assets Acquired Value	-	-	-	1.5	1.1	6.2	7.2	0.6	1.0
Total Loans and Investment at Cost	-	68.6	244.7	589.2	897.5	1,270.4	2,217.4	3,410.2	3,890.6
Total Loans and Investment Value	-	77.2	280.9	670.5	1,025.6	1,502.5	4,809.2	4,562.0	3,892.8
Loans and Investments Net of Current Maturities	-	76.9	280.7	670.2	1,024.7	1,499.2	4,803.4	4,556.5	3,887.7
Total Other Assets	-	3.7	9.6	16.2	19.6	23.7	33.6	62.3	72.8
TOTAL ASSETS	-	122.7	476.6	956.1	1,348.8	1,756.4	5,223.3	5,035.3	4,356.3
LIABILITIES AND CAPITAL									
Liabilities									
Current Liabilities	-	6.0	2.2	1.7	4.5	25.4	21.9	49.5	62.3
Other Liabilities	-	0.0	1.0	0.8	0.1	0.1	4.8	20.4	23.3
Long-Term Debt									
SBA Notes and Debentures Payables	-	9.0	9.0	11.0	11.0	7.3	10.2	21.8	33.9
Other Notes and Debentures Payable	-	4.7	-	-	-	0.0	-	-	-
Total Long-Term Debt	-	13.7	9.0	11.0	11.0	7.3	10.2	21.8	33.9
Total Liabilities	-	19.7	12.2	13.4	15.6	32.8	36.8	91.7	119.5
Total SBA Participating Securities	-	6.0	254.1	537.0	730.7	882.5	1,489.8	2,065.5	2,648.9
Total Private Contributed Capital	-	98.9	198.1	343.3	503.7	671.7	1,111.5	1,793.9	2,092.2
3% SBA Preferred Stock Purchased by SBA	-	-	-	-	-	-	-	-	-
Other Capital Adjustments	-	-	-	-	-	(0.0)	(5.6)	(15.9)	(16.7)
Unrealized Gain (Loss) on Securities held	-	8.5	35.2	81.2	130.4	231.8	2,591.8	1,152.3	3.2
Undistributed Realized Earnings	-	(10.4)	(22.9)	(18.9)	(29.6)	(59.4)	(1.0)	(52.3)	(490.8)
TOTAL LIABILITIES AND CAPITAL	-	122.7	476.6	956.1	1,348.8	1,756.4	5,223.3	5,035.3	4,356.3

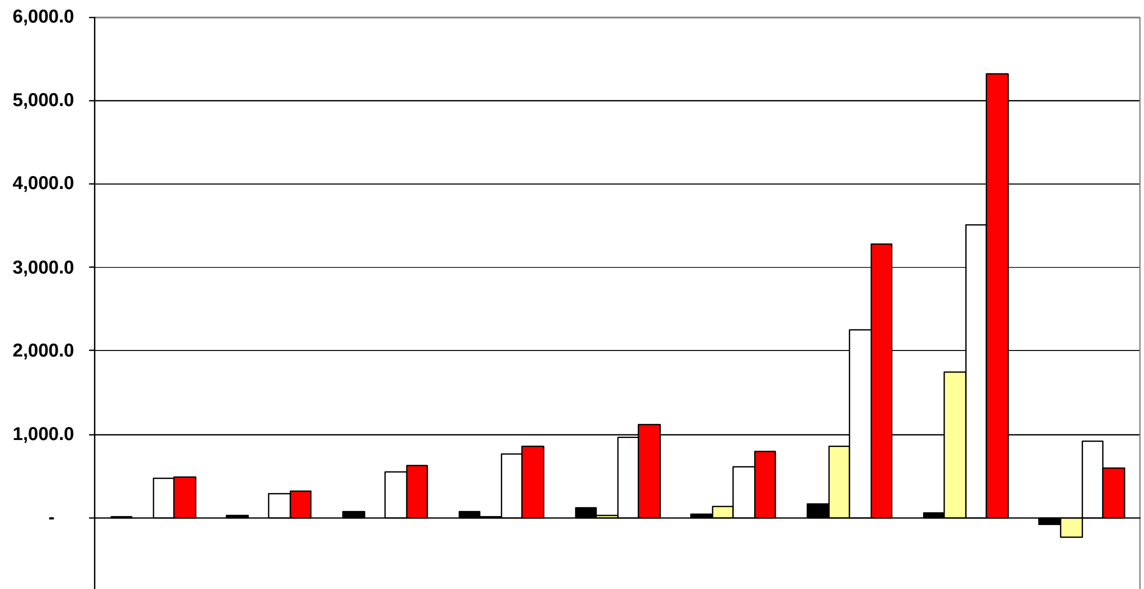
[35] The data reflects the annual 468s received in each FY for SBICs still active by the end of each FY. It does not include any SBICs that were transferred to Liquidations or surrendered licenses prior to the end of the FY.

5.2 Analysis of SBIC Licensee Financials

Net Income

Venture capital fund performance is driven by the market, as the trends indicate on the chart below. Exhibit 30 charts SBIC Licensees' net income by type of fund. To provide further insight, the chart separates debenture and bank-owned SBICs.[36]

Exhibit 30 – SBIC Licensee Net Income ($ Millions) by Fiscal Year[37]



Fiscal Years	1994	1995	1996	1997	1998	1999	2000	2001	2002
Debenture/SSBIC	13.0	26.3	71.3	69.3	121.0	51.1	172.5	59.0	(79.3)
Participating	-	(0.6)	(0.8)	18.6	29.6	131.2	856.1	1,739.3	(233.4)
Bank-Owned	474.4	292.8	557.6	762.3	962.8	611.6	2,258.4	3,518.2	912.8
Total	487.3	318.5	628.1	850.2	1,113.4	793.9	3,287.0	5,316.4	600.2

A few highlights are noted below:

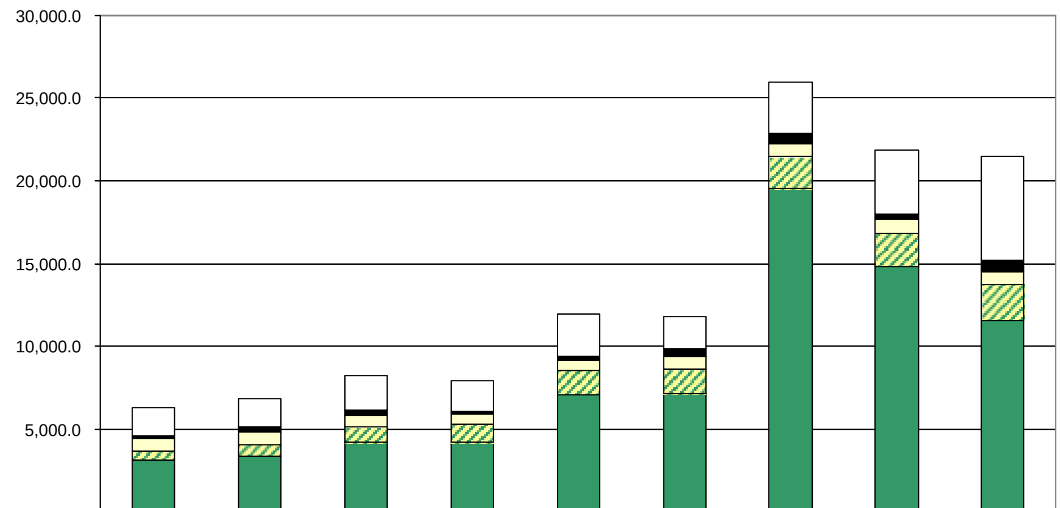
- Combined net income totaled $13.4 billion from FY 1994 through 2002.
- Bank-owned licensees provide the largest contribution to net income during FY 1994 through 2002, earning $10.4 billion in net income.
- Participating securities licensees provided the next largest contribution, with $2.5 billion during this timeframe. Debenture licensees provided $0.5 billion.
- All fund types suffered decreases in FY 2002, with only bank-owned SBICs contributing positive net income, resulting in a combined licensee net income of $600 million.

[36] SSBICs, while a part of the consolidated debenture financials, are no longer being licensed and are small enough that they do not show up on graphs in comparison to the rest of the program. Therefore they have been included within the debentures in this analysis.
[37] The data reflects the annual 468s received in each FY for SBICs still active by the end of each FY. It does not include any SBICs that were transferred to Liquidations or surrendered licenses prior to the end of the FY. It should be noted that net incomes do not include unrealized appreciation or depreciation.

Assets

A breakdown of the combined assets for SBIC Licensees is shown in the exhibit below.

Exhibit 31 – SBIC Licensee Assets at Value FY 1994 through FY 2002
($ Millions)[38]



Fiscal Years	1994	1995	1996	1997	1998	1999	2000	2001	2002
Current Assets	1,710.9	1,722.0	2,147.0	1,871.3	2,590.0	1,899.8	3,129.5	3,898.1	6,332.2
Other Assets	114.61	265.56	241.32	145.08	216.24	524.79	658.10	313.10	668.51
Loans	769.3	767.6	766.5	635.2	614.2	762.1	778.3	863.9	744.5
Debt Securities	547.7	730.7	925.7	1,092.7	1,453.2	1,486.8	1,943.4	1,956.5	2,201.1
Equity Securities	3,120.9	3,340.4	4,159.1	4,172.2	7,075.8	7,110.9	19,487.0	14,824.7	11,550.2
Total Assets	6,263.4	6,826.3	8,239.6	7,916.5	11,949.4	11,784.4	25,996.3	21,856.3	21,496.6

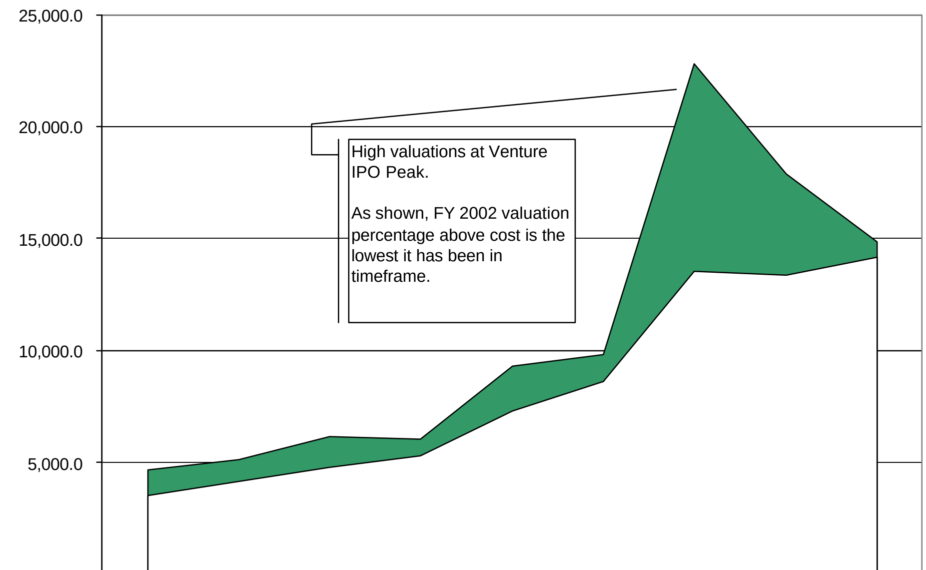
A few observations are noted below:

- Total assets reached their peak in FY 2000 with almost $26 billion in assets, of which 75% were equity securities.
- With the decline in the stock market and resulting lowering of valuations, by FY 2002, assets declined to $21.5 billion, still almost twice the assets from FY 1999.
- By FY 2002, current assets (including cash) rose to 29% of total assets and equity securities declined to 54% of total assets.
- The 41% decline in equity securities from FY 2000 to FY 2002 may be attributed to a decline in valuations of securities from the FY 2000 peak, causing significant reductions in unrealized gains as shown in the chart on the next page.

[38] The data reflects the annual 468s received in each FY for SBICs still active by the end of each FY. It does not include any SBICs that were transferred to Liquidations or surrendered licenses prior to the end of the FY.

As shown in the next chart, recent valuations appear to be more conservative as the overall value to cost ratio in FY 2002 is the lowest it has been during this timeframe.

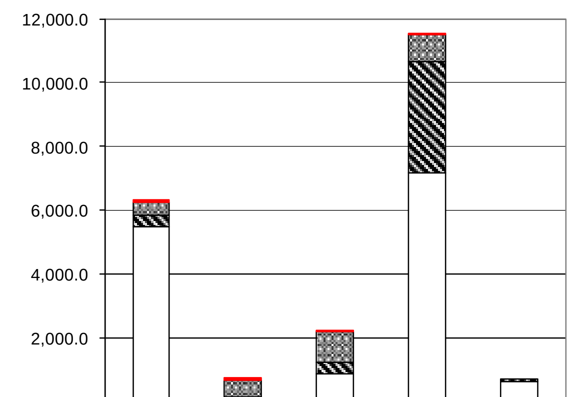
Exhibit 32 – SBIC Licensee Loans and Investments Cost vs. Value FY 1994 through 2002 ($ Millions)[39]



Fiscal Years	FY 1994	FY 1995	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002
Total Loans & Investments at Value	4,653.4	5,116.7	6,136.6	6,040.6	9,319.6	9,819.3	22,805.7	17,879.2	14,874.8
Total Loans & Investments at Cost	3,523.5	4,178.1	4,778.4	5,294.4	7,325.1	8,644.4	13,554.8	13,395.8	14,169.8
Percent above Cost	32%	22%	28%	14%	27%	14%	68%	33%	5%

- Exhibit 33 depicts the distribution of assets by fund type (participating, debenture, SSBIC, and bank-owned). As shown, the bank-owned contribute the highest in all categories except loans.
- While bank-owned hold the most equity securities, participating funds hold more proportionately.
- The large increase in FY 2002 in current assets is primarily attributed to bank-owned funds.

Exhibit 33 – FY 2002 Assets by Fund Type ($ Millions)[30]



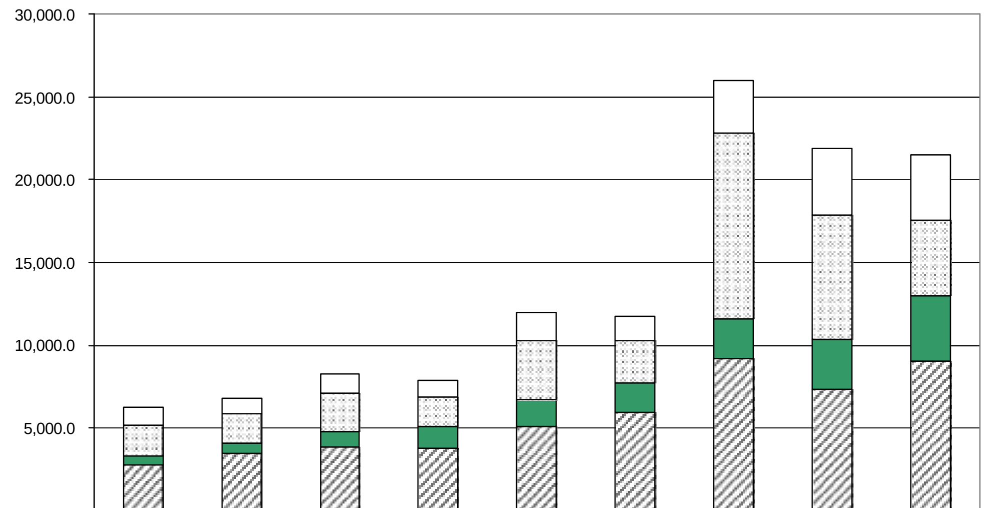
	Current Assets	Loans	Debt Securities	Equity Securities	Other Assets Less Current Maturities	Total Assets
SSBIC	72.0	87.3	17.1	33.2	(12.3)	14,200.2
Debenture	402.8	525.3	973.4	870.7	(29.4)	4,356.3
Participating	395.8	55.0	348.2	3,468.8	88.6	2,742.8
Banks	5,461.6	77.0	862.6	7,177.4	621.6	197.3
TOTAL	6,332.2	744.5	2,201.1	11,550.2	668.5	21,496.6

[39] The data reflects the annual 468s received in each FY for SBICs still active by the end of each FY. It does not include any SBICs that were transferred to Liquidations or surrendered licenses prior to the end of the FY.

Liabilities and Capital

On the other side of the balance sheet, we can see how investments were financed through liabilities and capital.

Exhibit 34 – SBIC Licensee Liabilities and Capital FY 1994 through 2002 ($ Millions)[40]



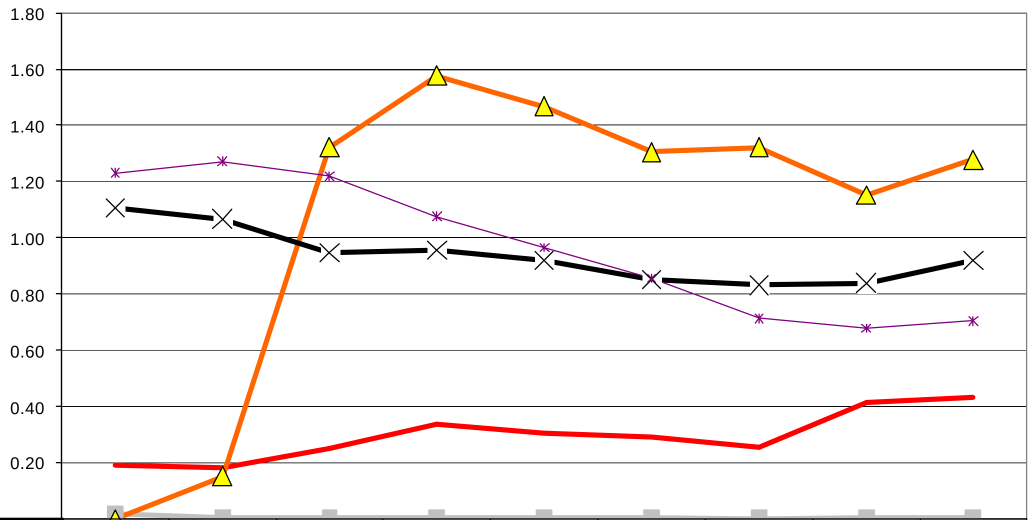
Fiscal Years	1994	1995	1996	1997	1998	1999	2000	2001	2002
Current and Other Liabilities	1,069.0	950.2	1,140.0	1,013.4	1,678.1	1,518.6	3,217.3	3,989.8	3,918.7
Other Capital Adjustments	1,861.9	1,796.5	2,316.8	1,808.7	3,595.7	2,541.5	11,207.0	7,492.0	4,611.3
SBA Leverage	533.9	627.6	952.3	1,284.4	1,555.6	1,751.1	2,363.3	3,047.9	3,929.3
Private Capital	2,798.6	3,452.0	3,830.5	3,810.8	5,129.0	5,973.1	9,208.9	7,326.6	9,037.3
Total Liabilities and Capital	6,263.4	6,826.3	8,239.6	7,917.2	11,958.4	11,784.3	25,996.3	21,856.3	21,496.6

- "Other Capital Adjustments," which includes unrealized gains in securities held, provided the largest contribution in FY 2000, 43% of all liabilities and capital. As the chart indicates, this declined to 21% by FY 2002, more in line with years prior to FY 2000.
- "Current and Other Liabilities," have increased to 18% of total liabilities and capital in FY 2002, up from an average of 14%.

[40] The data reflects the annual 468s received in each FY for SBICs still active by the end of each FY. It does not include any SBICs that were transferred to Liquidations or surrendered licenses prior to the end of the FY.

SBA Leverage has steadily increased and become a larger part of capital since 1994. Since SBICs may be eligible for SBA leverage in an amount up to three times private capital for debentures and two times private capital for participating securities, it may be surprising that private capital outweighs SBA leverage. The chart below drills down by fund type on this ratio to understand the differences.

Exhibit 35 – SBIC Licensee Outstanding Leverage to Private Capital Ratio by Fiscal Year[41]



Fiscal Years	1994	1995	1996	1997	1998	1999	2000	2001	2002
Overall	0.19	0.18	0.25	0.34	0.30	0.29	0.26	0.42	0.43
Banks	0.02	0.00	0.00	0.01	0.00	0.00	0.00	0.00	0.01
Participating	-	0.15	1.32	1.58	1.47	1.30	1.32	1.15	1.28
Debenture	1.11	1.07	0.95	0.96	0.92	0.85	0.83	0.84	0.92
SSBICs	1.23	1.27	1.22	1.08	0.96	0.86	0.71	0.68	0.70

- While the combined SBA leverage to private capital ratio is only .43, this is due to the bank funds which take very little SBA leverage in comparison to the private capital they provide.
- Participating securities maintained the highest ratio at 1.28 in FY 2002.
- As more participating security funds are licensed and utilize the SBA leverage, the overall ratio will be driven higher, as it has steadily done since FY 1994. This indicates that the SBA will be incurring additional risk.
- While participating securities (not including additional debentures) provided over 50% of the capital in the participating security funds, it is interesting to note that given the cumulative net income (before non-recurring items and accounting adjustments) for participating securities licensees of $2.5 billion, the SBIC program only received $281 million in profit participation (about 11% of profits).

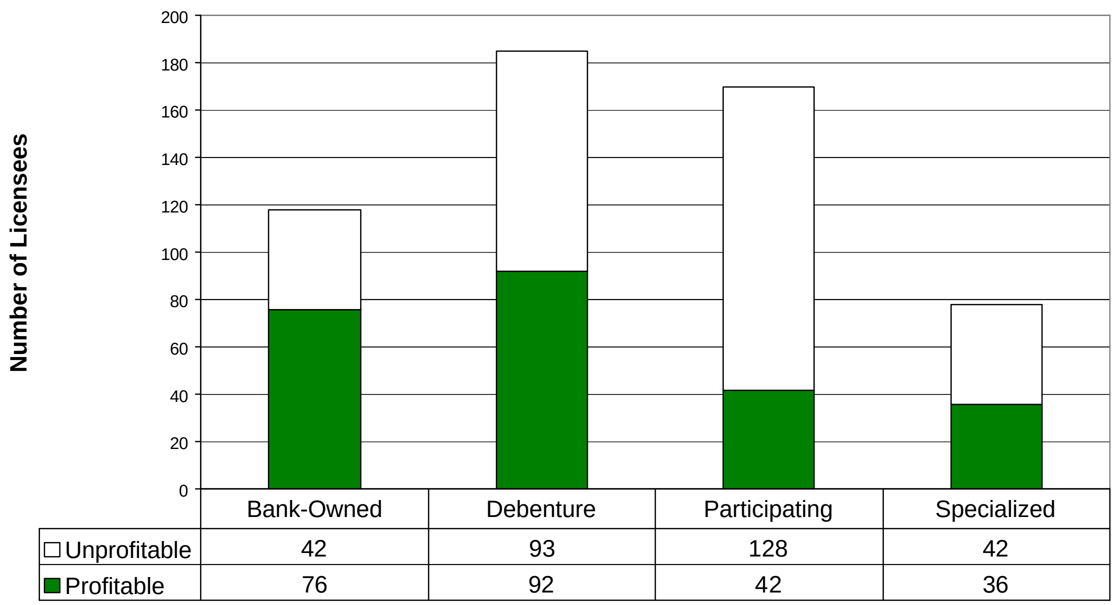
However, this last statement highlights the weaknesses of looking at financial statements on a consolidated basis alone. This is because the SBA's profit participation is based only on profitable SBICs, while the consolidated net income incorporates SBICs with losses as well. The following exhibit provides a breakdown of SBICs by fund type, separating profitable from unprofitable (based on sum of net income between the period of FY 1994 and FY 2002). As shown, the

[41] The data reflects the annual 468s received in each FY for SBICs still active by the end of each FY. It does not include any SBICs that were transferred to Liquidations or surrendered licenses prior to the end of the FY.

SBA's profit participation is only 9.1% of profitable SBIC licensees' net income. While consolidated licensee numbers give us some information, funds must be looked at on an individual basis.

Exhibit 36 – SBIC Profitable versus Unprofitable SBIC Licensees[42]

Profitable versus Unprofitable SBICs (FY 1994 through FY 2002)



FUNDTYPE	Profitable Net Income ($M)	Profitable Number	Unprofitable Net Loss ($M)	Unprofitable Number	Total Net Income ($M)	Total Number	% Number Profitable
Bank-Owned	10,476.4	76	(374.7)	42	10,101.7	118	64.4%
Debenture	619.2	92	(168.3)	93	450.9	185	49.7%
Participating	3,095.8	42	(595.9)	128	2,500.0	170	24.7%
Specialized	62.8	36	(28.3)	42	34.5	78	46.2%
TOTAL	14,254.2	246	(1,167.1)	305	13,087.1	551	44.6%

SBA Profit Participation	$	280.7 M
% of Profitable Participating Securities Net Income		9.1%
% of Total Participating Securities Net Income		11.2%

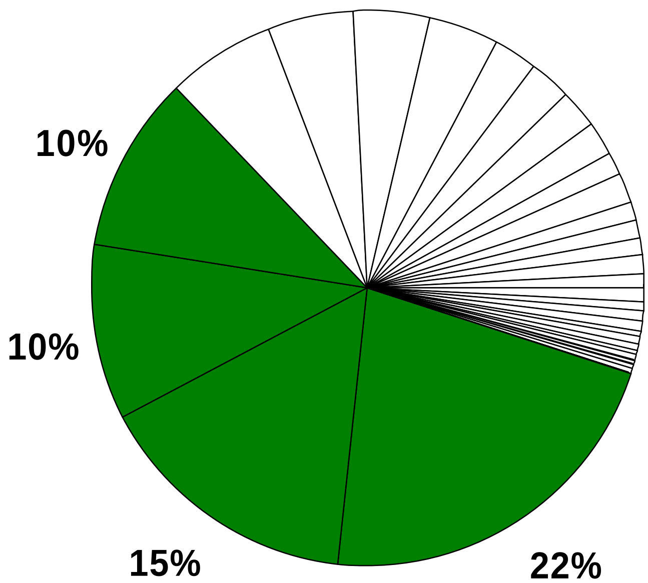
As one can see, the data on participating securities licensees indicates that only 24.7% of such licensees were profitable (the lowest percentage profitable group by fund type), although such licensees represented the second highest group net income during this timeframe. This indicates a large degree of variance within the group. Exhibit 37 shows that while 42 of the participating securities licensees distributed profit participation, over 50% of the $280.7 million were by 4 funds and 90% of the $280.7 million were by only 14 of the funds.

[42] The data reflects the annual 468s received in each FY for all SBICs, including any transferred to Liquidations or surrendered licenses prior to the end of the FY. However, not all SBICs in liquidations maintain 468 data. Therefore, this may not include the entire performance of a fund during this timeframe. It should be noted that net incomes do not include unrealized appreciation or depreciation.

Exhibit 37 – SBICs Providing Profit Participation (FYs 1994 through 2002)[43]

Profit Participation by 42 Licensees

4 Provided over 50% of Profit Participation
14 Provided over 90% of Profit Participation



Total Profit Participation (FYs 1994 through 2002): $280.7M

[43] The data is retrieved from the Distributions Table maintained by Data Management through FY 2002.

Appendix A – Glossary of Terms

Term	Definition for Purposes of This Report
Business Plan	Document which describes a company’s plans, normally addressing products/services offered, market and competition, operations, management team, past and projected financials, and exit strategies. This document is usually used to help raise capital for the company.
Capital Call	Event in which a venture/SBIC fund requests that its investors fund some or all of their capital commitments.
Capital Structure	A company’s mix of different securities, including loans, debt securities, and equity securities.
Carry / Carried Interest	Share of a venture/SBIC fund's profit that goes to the general partners/managers of the fund, providing an incentive for the managers.
Commitments / Committed Capital	Capital committed by investors to a venture/SBIC fund indicating the maximum amount the fund may draw down from the investor.
Debentures	Debt obligations issued by Licensees pursuant to section 303(a) of the Act and held or guaranteed by SBA.
Debt Security	A financing agreement/security that includes both equity and debt features (e.g., loan with warrants or convertible debt)
Disbursement	Leverage actually disbursed by the SBIC program.
Distribution	Any transfer of cash or non-cash assets to SBA, its agent or Trustee, or to partners in a Partnership Licensee, or to shareholders in a Corporate Licensee. Capitalization of Retained Earnings Available for Distribution constitutes a Distribution to the Licensee's non-SBA partners or shareholders.
Due Diligence	The process by which a potential investor investigates, examines, and verifies a business and its management prior to investment.
Equity Security	Stock of any class in a corporation, stock options, warrants, limited partnership interests in a limited partnership, membership interests in a limited liability company, or joint venture interests.

Term	Definition for Purposes of This Report
Exit Strategy	How a company intends to provide liquidity to its investors. This may sometimes be accomplished through an initial public offering or a sale to a strategic buyer.
J-Curve	Refers to venture capital's typical investment cycle in which returns tend to be negative for a few years at the beginning of a fund's investment cycle before eventually rising through investment gains both realized and unrealized.
Leverage	Financial assistance provided to a Licensee by SBA, either through the purchase or guaranty of a Licensee's Debentures or Participating Securities, or the purchase of a Licensee's Preferred Securities, and any other SBA financial assistance evidenced by a security of the Licensee.
Limited Partnership	A partnership consisting of one or more general partners and one or more limited partners. Limited partners normally provide the financing of the partnership with little responsibility in terms of management or personal liability. General partners are responsible for managing the entity with liability for its debts. Approximately two-thirds of SBICs are organized as limited partnerships.
LMI Zone	Any area located within a HUBZone (as defined in 13 CFR 126.103), an Urban Empowerment Zone or Urban Enterprise Community (as designated by the Secretary of the Department of Housing and Urban Development), a Rural Empowerment Zone or Rural Enterprise Community (as designated by the Secretary of the Department of Agriculture), an area of Low Income or Moderate Income (as recognized by the Federal Financial Institutions Examination Council), or a county with Persistent Poverty (as classified by the Economic Research Service of the Department of Agriculture).
Loan	A transaction evidenced by a debt instrument with no provision for the licensee to acquire Equity Securities.
Management Assessment Questionnaire	SBA evaluation form with a series of structured questions concerning management's plans for the prospective SBIC and the detailed experience and qualifications of the management team.
Management fees	Usually an annual charge paid to the managers of the venture/SBIC fund for the fund's operations.
NASBIC	National Association of Small Business Investment Corporations. Professional association of Small Business Investment Companies (SBIC) and other venture capitalists.
Paid-in Capital	The amount of capital that private investors have actually paid into the fund.

Term	Definition for Purposes of This Report
Participating Securities	Preferred stock, preferred limited partnership interests, or similar instruments issued by licensees, including debentures having interest payable only to the extent of earnings, all of which are subject to the terms set forth in 13 CFR Secs. 107.1500 through 107.1590 and section 303(g) of the Act.
Portfolio Company/Concern	Company to which a venture/SBIC fund has provided financial assistance.
Prioritized Payments	A cumulative preferred return on participating securities, which is contingent upon the profitability of the SBIC and which is passed through to the certificate holders. The SBA advances prioritized payments to certificate holders and is repaid when SBICs are profitable.
Private Capital	The contributed capital of a licensee, plus unfunded binding commitments by Institutional Investors (including commitments evidenced by a promissory note) to contribute capital to a licensee.
Profit Participation	Amount payable to SBA in consideration for SBA's guarantee of the SBICs' Participating Securities.
SBA Form 1031	Reports submitted by the SBICs containing financing information. For each Financing of a Small Business (excluding guarantees), licensees must submit a Portfolio Financing Report on SBA Form 1031 within 30 days of the closing date.
SBA Form 468	Reports submitted by the SBICs, containing financial and supplementary information on the SBIC. Forms are required to be submitted annually, but may be requested by the SBA more frequently.
Seed/Start-Up	Seed/Start-Up Stage[44]: The initial stage. The company has a concept or product under development, but is probably not fully operational. Usually in existence less than 18 months.
Stage	Indicates the stage in development of a company. The following definitions are taken from the PriceWaterhouseCooper (PWC) MoneyTree website (www.pwcMoneyTree.com): Seed/Start-Up Stage: The initial stage. The company has a concept or product under development, but is probably not fully operational. Usually in existence less than 18 months.

[44] Definition taken from the PriceWaterhouseCooper (PWC) MoneyTree website (www.pwcMoneyTree.com):

Term	Definition for Purposes of This Report
	Early Stage: The company has a product or service in testing or pilot production. In some cases, the product may be commercially available. May or may not be generating revenues. Usually in business less than three years.
	Expansion Stage: Product or service is in production and commercially available. The company demonstrates significant revenue growth, but may or may not be showing a profit. Usually in business more than three years.
	Later Stage: Product or service is widely available. Company is generating on-going revenue; probably positive cash flow. More likely to be, but not necessarily profitable. May include spin-outs of operating divisions of existing private companies and established private companies.
Surrender	Action by SBIC licensee to return its license to the SBA. An SBIC may not surrender its license without SBA's prior written approval.
Valuation	The value of a company/business. In private equity, valuations are normally determined based on financings by a sophisticated investor with no prior relationships with the company. All SBICs are required to have valuation guidelines to reassess company valuations at least annually.
Vintage Year	Usually indicates the year the first investment or capital call was made for the fund.

Appendix B – Description of Projected Losses Calculation

Projected losses are estimated first in the "liquidations" portfolio, and then in the "active" portfolio as follows:

- Liquidations Portfolio Projected Losses:
  - The Office of SBIC Liquidations performs an estimate of all projected net recoveries for all outstanding leverage that has been transferred to its office at the end of each fiscal year. The assets of an SBIC from which the SBA will seek to recover the leverage may include outstanding equities, debt securities, notes, or tangible property as well as any investment instrument an SBIC might have utilized in providing financing. At that time, using a detailed bottoms-up approach, on an asset by asset basis, the office reviews the recoverable value of the asset based on valuations, estimates, and appraisals as well as payment history, security, and other pertinent and available information dependent upon the type of holding, the priority of the investment, and the overall market conditions. The Office of SBIC Liquidations reassesses this estimate each year.
  - Since it applies to the outstanding leverage in the Liquidations Portfolio, the total projected loss estimate appears in the balance sheet. To maintain the correct loss reserve, the change to this amount appears in the P&L.
  - In comparing Total Projected and Actual Losses to the Gross Transferred Leverage in the Balance sheet through FY 2002, historically, about 63% of all leverage transferred into Liquidations is anticipated to be recovered. Prioritized payments transferred into Liquidations only project a 19% recovery rate, as these payments are contingent capital based on SBIC profits.

- Projected losses are estimated in the "active" portfolio as follows:
  - Losses in the Active Portfolio are estimated using the equation below. The calculation is based on an estimated default rate multiplied by an estimated loss rate multiplied by outstanding leverage plus advances. SSBICs are calculated separately from SBICs.

Projected Losses in Active Portfolio = (Outstanding Leverage + Outstanding Advanced Prioritized Payments) x Default Rate x Loss Rate

where

$$\text{Default Rate} = \frac{\text{Amount of Cash Defaulted}}{\text{Total Cash Disbursed}} = \frac{\text{Leverage + Advances Transferred to Liquidations}}{\text{Totals Disbursements + Advances}}$$

$$\text{*Loss Rate} = \frac{\text{Projected Current Losses in Liquidations}}{\text{Amount of Cash Defaulted}} = \frac{\text{Projected Losses in Liquidation}}{\text{Leverage + Advances Transferred to Liquidations}}$$

*Note on Loss Rate Equation: The "Projected Losses in Liquidation" figure is based on the estimate from the liquidations/restructurings portfolio, discussed above. The "Leverage + Advances Transferred to Liquidations/Restructurings" figure only includes cases that are still open.

  - As with Projected Losses in Liquidations, since this number applies to the outstanding leverage in the Active Portfolio, the resulting estimate appears in the balance sheet. The change to this amount each year appears in the P&L. The following chart looks at the projected losses estimated by this calculation over time.