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SBA Views on “Measuring the Role of the SBIC Program in Financing Small Businesses”

In 2015, SBA contracted with the Federal Research Division, Library of Congress (FRD) to conduct a study to establish a better understanding of the role the SBIC program has played in providing financing to the small business sector over the last 20 years. The results of the FRD study were submitted to SBA in July 2017.

After reviewing the submission, SBA has identified a number of weaknesses and limitations in the underlying data and methodology that may cause the study’s conclusions to be misleading. SBA is posting this Disclaimer Notice to prevent any misunderstandings by the reader.

- Unvalidated Data. The data used by FRD was provided to FRD by SBA “AS IS”, without any representation or warranty, express or implied, with respect to the content, completeness, or accuracy of the information provided. SBA continues to make no representation or warranty regarding such data. Accordingly, the study’s conclusions are subject to question given the uncertainty concerning the reliability of the data.
- Limited Timeframe Analyzed. The study was intended to analyze a full twenty-year period between 1995 and 2015. For a number of reasons, the researchers analyzed only six years of data – from 2010 through 2015. Accordingly, rather than drawing conclusions based on two decades worth of data, the evaluation focused exclusively on a six-year period that represented one of the strongest periods of economic expansion in U.S. history. SBA cannot be certain that the study’s conclusions are not skewed, whether in minor or potentially significant ways, by data that is not representative of the program. As a result, it may not be appropriate to extrapolate from the study any meaningful conclusions about the broader impact of the SBIC program.
- Undisclosed External Data Sources and Methodology. The study discloses that the data was supplemented by interviews with several investors in SBICs as well as surveys. However, no interview or survey questions are included in the study and only a very limited portion of the feedback received during the interviews is summarized. In addition, no interviews were conducted of investors who invest exclusively in non-SBIC investment funds. The select use of this anecdotal information to support the study’s conclusions may suggest a level of certainty that is not warranted.
- Limited Weight Given to Weaknesses. The study briefly discloses certain weaknesses in two paragraphs under the vague heading “Research Notes”, which the authors have included “to, potentially, allow the reader to draw different conclusions.” The stated weaknesses include incomplete data on “funds, deals and investee businesses” as well as inconsistent definitions of variables – all of which represent the foundation of the study’s analysis and conclusions. The disclosure also alludes to the unavailability of non-SBIC data from private firms. Together, these weaknesses, which are given minimal weight and visibility in the study, raise questions about the validity of the study’s conclusions.



Measuring the Role of the SBIC Program in Financing Small Businesses

*A Report Prepared by the Federal Research Division,
Library of Congress
under an Interagency Agreement with the
Office of Investment and Innovation,
U.S. Small Business Administration*

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PREFACE

The U.S. Small Business Administration (SBA) oversees the Small Business Investment Company (SBIC) program, which provides an alternative source of financing for small businesses lacking access to adequate capital from traditional sources. Since the program's inception in 1958 through December 2015, SBICs have deployed US\$80.5 billion in capital (one-third from the private sector) into approximately 172,800 financings.¹

The goal of this report is to contribute to a deeper understanding of the role the SBIC program has played in providing financing to the small business sector using data collected exclusively by the SBA under the SBIC program. The report addresses key questions concerning the role the SBIC program plays in the overall financial industry.

The SBA's Office of Investment and Innovation (OII) contracted with the Federal Research Division (FRD) of the Library of Congress for an independent evaluation of the SBIC program. FRD provides customized research and analytical services on domestic and international topics to agencies of the U.S. government, the government of the District of Columbia, and authorized federal contractors on a cost-recovery basis.

FRD enlisted the aid of two experienced scholars with particular expertise in financial markets to perform this research:

- Dr. John Paglia, an associate dean and professor of finance at Pepperdine University's Graziadio School of Business and Management. Dr. Paglia founded and directed the Pepperdine Private Capital Markets Project, which examined, among many other things, the demand for capital by and financing success rates for business owners. The project also examined investments by private equity groups, venture capital firms, and mezzanine funds (among more than a dozen other types of financing), including activity in the lower-middle market, which is defined as the market segment containing businesses with between US\$5 million and US\$100 million in annual revenues.

¹ U.S. Small Business Administration (SBA), *Offering Circular: Guaranteed 2.507% Debenture Participation Certificate, Series SBIC 2016-10 A*, March 14, 2016, 7, https://www.sba.gov/sites/default/files/SBIC_2016-10Acusip-831641-FF7.pdf.

- Dr. David T. Robinson, a professor of finance and the J. Rex Fuqua Distinguished Professor of International Management at Duke University and a research associate at the National Bureau of Economic Research. Dr. Robinson has published several papers in the fields of entrepreneurial finance, venture capital, and private equity, and has conducted a number of studies that analyze the conditions and performance of the financial sector serving young and small businesses, both on the equity and debt side.

The analysis in this report is based on 1995–2015 SBIC data from SBA Portfolio Financing Report (SBA Form 1031) filings, which are submitted by SBICs within 30 days of closing on a financing, and SBA Annual Financial Report (SBA Form 468) filings, which are audited and submitted by SBICs annually. The authors used personal interviews, surveys, and external data sources to augment and validate the data where possible to build the fullest picture possible of the investment behavior of SBIC funds.

This report represents an independent analysis by FRD and the authors, who have sought to adhere to accepted standards of scholarly objectivity. It should not be construed as an expression of an official U.S. government position, policy, or decision.

The SBA makes no representation as to the analysis or calculations performed by the Library of Congress or its employees or contractors and reported in this study. The SBA has not verified the analysis or calculations performed in this study. This study was conducted by third parties not affiliated with the SBA and is intended to be independent from the SBA.

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OVERVIEW OF FINDINGS

One of the core missions of the U.S. Small Business Administration (SBA) is to help Americans start, build, and grow their own businesses. The SBA’s Small Business Investment Company (SBIC) guaranteed loan program assists in these efforts by harnessing “the talent of professional investment fund managers to identify and finance promising small businesses.”² These small businesses support jobs across a diverse set of industries, including business-to-business (B2B), business-to-consumer (B2C), energy, financial services, healthcare, information technology (IT), and materials and resources.³ For this reason, the SBA approached the Library of Congress’s Federal Research Division (FRD) to assess the SBIC program’s role in the overall financial industry by:

1. Examining how the SBIC program fits into and compares with the overall financial industry, with a particular focus on:
 - The role SBICs play in the financing environment for small businesses,
 - Whether SBIC program investments target different industries than non-SBIC private equity funds, and
 - Whether SBIC program investments target broader communities than non-SBIC private equity funds.
2. Exploring the question of whether SBICs add any other tangible or intangible value not provided by non-SBIC private equity funds.

Drawing on statistical analysis of relevant business data from the SBA and other sources, the authors found that the SBIC program is not only widely diversified by industry sector and geographic subregion, but varies from non-SBIC private equity funding on key dimensions concerning the companies, industries, and regions receiving investments. For example,

² SBA, *The Small Business Investment Company (SBIC) Program Overview*, last updated February 24, 2016, https://www.sba.gov/sites/default/files/files/SBIC_Program_Executive_Summary_2016.pdf.

³ Business-to-business industries are those in which one business makes a commercial transaction with another one. This typically occurs when a business is sourcing materials for its production process (e.g., a food manufacturer purchasing salt), a business needs the services of another for operational reasons (e.g., a food manufacturer employing an accounting firm to audit its finances), or a business re-sells the goods and services produced by another (e.g., a retailer purchasing products from a food manufacturer). Business-to-consumer industries are those in which transactions are conducted directly between a company and the consumers who are the end-users of its goods and services.

- **SBIC investments support companies that are less likely to be considered by private equity investors.** SBICs invest in companies that are smaller than those funded by traditional private equity sources of similar size and investment focus. Because they are smaller, investing in these companies is typically less attractive to larger private equity investors.
- **SBIC investments fund different sectors than the rest of the private equity universe.** As a group, SBICs deployed the largest concentration of dollars—nearly half—to the B2B sector, more than double the share invested by the overall investment community. SBICs also invested considerably less in other sectors traditionally favored by the broader financial industry, including the B2C sector, which SBICs funded at half the rate of the overall investment community. Moreover, SBICs invested far less in sectors with high capital requirements, like energy and healthcare, than traditional funding sources.
- **SBIC investments spread capital in a more dispersed manner across the country than traditional investors.** The SBIC program funds deals that are more widely geographically distributed than the broader investment fund community, both in terms of the proportion of deals by region and the proportion of dollars invested by region. Displaying a far lower concentration of capital on the West Coast, the majority of SBIC funds invest in traditionally underserved regions of the United States, particularly Kansas, Minnesota, Nebraska, North Dakota, and South Dakota in the northern Midwest, and Alabama, Kentucky, Mississippi, and Tennessee in the South.

Altogether, these findings show the tangible value SBIC funds provide as a robust source of financing for small businesses in the U.S. economy. As compared to the broader financing landscape for small and mid-sized businesses—where over 35,000 deals were made and over US\$1.5 trillion was invested—SBICs have higher capital distribution ratios among small businesses and distribute capital more evenly among nine geographic subregions.⁴

Available data shed less light on the issue of whether SBICs add intangible value not otherwise provided by non-SBIC private equity funds. Inherently a subjective question, addressing the relative value of SBIC funding compared to pure private equity funds from a quantitative perspective would require knowledge not only about how deals are made, but also information about how these deals compare to investments not made. Given the closely held nature of such data in private financial transactions, the authors were unable to provide conclusive, independent

⁴ Due to the lack of public disclosures for private equity and related funds, it is difficult to directly access or assemble a comprehensive database of relevant information. For this analysis, the authors relied on custom reports provided by Pitchbook Data.

findings from a quantitative or statistical perspective. In addition, measuring intangible value would require data on intangible outcomes. Such data generally do not exist.

However, in previous reports prepared by the authors for the SBA’s Office of Investment and Innovation (OII), they found that the SBIC program stimulates business activity among the minority- and women-led business communities, and that it is an important source of capital for facilitating job creation for small businesses—which alone suggests that there may be important intangible value not otherwise provided by non-SBIC private equity funds.⁵

BACKGROUND ON THE SBIC PROGRAM

Description of SBICs

The SBA was established in 1953 to promote the development of small businesses by providing “loans, loan guarantees, contracts, counseling sessions and other forms of assistance.”⁶ The organization’s authorizing legislation was the Small Business Act, which created the agency to “aid, counsel, assist and protect, insofar as possible, the interests of small business concerns.” In 1958, the Small Business Investment Act created the SBIC program, under which the SBA “licensed, regulated and helped provide funds for privately owned and operated venture capital investment firms.”⁷ The U.S. government designed the program to provide debt and equity financing to high-risk small businesses lacking access to adequate capital from traditional sources.⁸ Since the program’s inception in 1958 through December 2015, participating SBICs have deployed US\$80.5 billion in capital (one-third from the private sector) into approximately 172,800 financings.⁹

⁵ John Paglia and David T. Robinson, *Measuring the Representation of Women and Minorities in the SBIC Program* (Washington, DC: Library of Congress, Federal Research Division [FRD], 2016), <https://www.sba.gov/sites/default/files/article-files/SBIC-Diversity-Report.pdf>; John Paglia and David T. Robinson, *Measuring the Role of the SBIC Program in Small Business Job Creation* (Washington, DC: Library of Congress, FRD, 2017), https://www.sba.gov/sites/default/files/articles/SBA_SBIC_Jobs_Report.pdf.

⁶ SBA, “History,” accessed April 7, 2016, <https://www.sba.gov/about-sba/what-we-do/history>.

⁷ 15 U.S.C. § 631(a), quoted in SBA, “History.”

⁸ SBA, *The Small Business Investment Company (SBIC) Program Overview*.

⁹ SBA, *Offering Circular: Guaranteed 2.507% Debenture Participation Certificate*, 7.

How SBICs Work

Fund managers submit applications to the SBA for a license to operate an SBIC. SBICs typically combine equity investments from private investors—such as pension funds, foundations, banks, and high-net-worth individuals—with government-guaranteed debt financing from the SBA. In the process, the SBICs leverage their equity capital, resulting in a capital structure (debt-plus-equity financing) that reduces the weighted average cost of capital and boosts returns on equity.

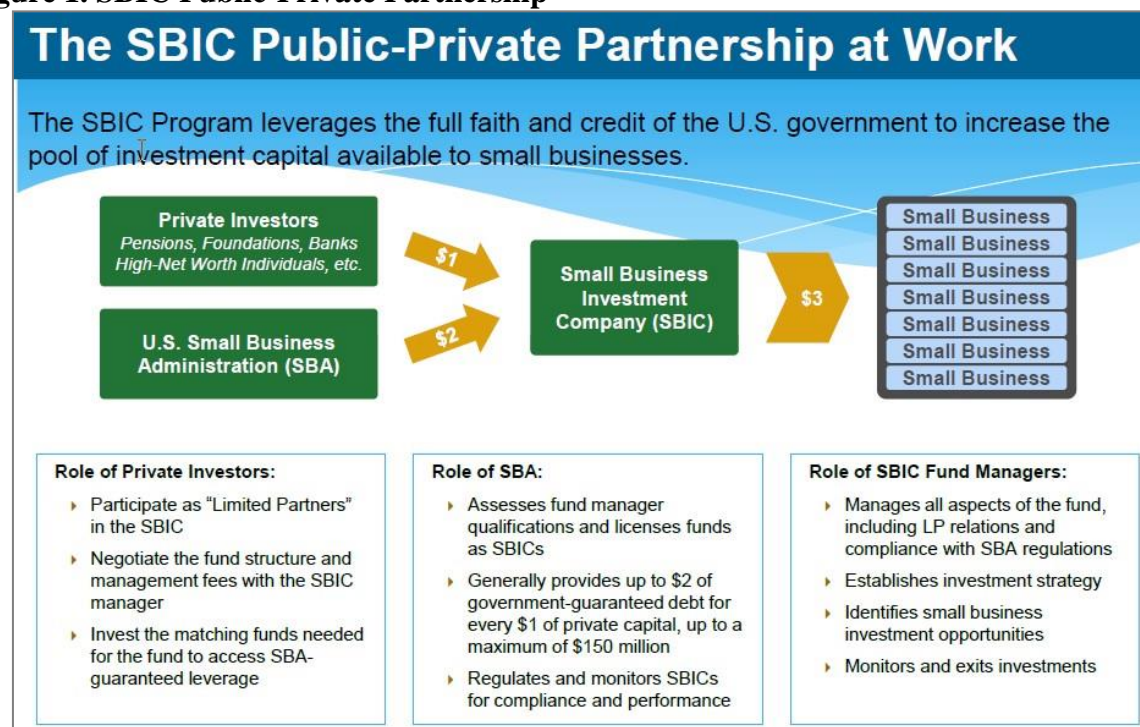
The Small Business Investment Act of 1958 enables the SBA to guarantee debentures issued by SBICs. Referred to by the SBA as “leverage,” the proceeds from these debentures are used to supplement an SBIC’s private capital, which in turn is used to make qualifying investments in small businesses. Through the SBA, the full faith and credit of the United States is pledged to guarantee timely payments of the principal and interest due on each debenture. An SBIC may issue debentures in an amount that is up to three times the amount of its private capital (although in most cases the limit is generally set at twice this amount). However, an SBIC may not issue more than \$150 million in debentures.¹⁰

The SBIC, typically formed as a limited partnership, invests in a portfolio of small businesses. When formed as a limited partnership, an SBIC—itself a limited partnership—has a general partner that manages the operations of the fund and limited partners who are passive investors. As the investments play out and the SBIC winds down, it repays its debt to the SBA and shares its profits with the investors (see fig. 1).¹¹

¹⁰ SBA, *Offering Circular: Guaranteed 4.084% Debenture Participation Certificates, Series SBIC 2011-10 A*, March 22, 2011, 5, https://www.sba.gov/sites/default/files/lender/SBIC%202011-10%20A%20831641EU5_0.pdf.

¹¹ SBA, *The Small Business Investment Company (SBIC) Program Overview*.

Figure 1. SBIC Public-Private Partnership



Source: "Bridging the Capital Formation Gap: The Small Business Administration's SBIC Program," Vimeo video, 57:07, from the Association for Corporate Growth, April 12, 2016, <https://vimeo.com/162594659>.

SBICs enable SBA-guaranteed leverage up to two times the amount of private capital, subject to caps of US\$150 million and US\$350 million for, respectively, individual funds and families of funds.¹² As a result, SBIC licensees are subject to various investment criteria. The most important criterion is that SBICs must invest in small businesses, which the SBA defines (solely for the purpose of the SBIC program) as those having less than US\$19.5 million in tangible net worth and an average net income for the preceding two years of less than US\$6.5 million. The SBA also considers small businesses that comply with the agency's size standards in terms of the number of employees or average annual receipts, as calibrated according to industry standards set out in the North American Industry Classification System (NAICS).¹³

¹² SBA, *The Small Business Investment Company (SBIC) Program Overview*.

¹³ Compliance with Size Standards as a Condition of Assistance, 13 C.F.R. § 107.700 (2009); What Size Standards are Applicable to Financial Assistance Programs?, 13 C.F.R. § 121.301 (2016); SBA, "Summary of Size Standards by Industry Standard," last updated February 26, 2016, <https://www.sba.gov/contracting/getting-started-contractor/make-sure-you-meet-sba-size-standards/summary-size-standards-industry-sector>.

The SBIC program is a particularly attractive investment target for the banking industry for two reasons. First, investments in SBICs are exempt from the Volcker Rule, a provision of the DoddFrank Wall Street Reform and Investor Protection Act that prohibits banks from owning hedge or private equity funds.¹⁴ Second, investments in SBICs may qualify for Community Reinvestment Act credits since they are presumed to promote the economic development of all members of a community, including residents of low- and moderate-income neighborhoods.¹⁵ Increased bank participation in the SBIC program in recent years has steadied investment demand, according to *American Banker* magazine.¹⁶

Currently Active SBICs

As of September 30, 2015—the end of the U.S. government fiscal year (FY)—there were 303 licensed SBICs, of which:

- 205 belonged to the ongoing debenture program (generally with a focus on later-stage, mezzanine, and buyout investments using primarily debt and hybrid financing),¹⁷
- 46 belonged to the discontinued participating securities program (with a high percentage of early-stage investments using equity financing),
- 43 belonged to the ongoing non-leveraged program (generally with a focus on later-stage, mezzanine, and buyout investments using primarily debt and hybrid financing), and
- 9 belonged to the discontinued specialized SBIC (SSBIC) program (with a focus on minority-, women-, and veteran-owned businesses using primarily loans).¹⁸

For a more detailed explanation of these SBIC programs, see “SBIC Funds” in the glossary in appendix I.

¹⁴ Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds, 79 Fed. Reg. 5535 (January 31, 2014).

¹⁵ Federal Deposit Insurance Corporation, “Interagency Questions and Answers Regarding Community Reinvestment,” last updated April 20, 2014, <https://www.fdic.gov/regulations/laws/rules/2000-6750.html>.

¹⁶ Shane Kite, “SBIC Revival: Why Interest from Banks is Way Up, As the Volcker Rule Looms,” *American Banker*, April 28, 2014, http://www.americanbanker.com/magazine/124_04/sbic-revival-why-interest-from-banks-is-wayup-as-the-volcker-rule-looms-1066822-1.html.

¹⁷ Five SBICs in this group were licensed under the SBA’s Early Stage SBIC Program, which was in effect from fiscal year 2012 through fiscal year 2016.

¹⁸ SBA, *Small Business Investment Company (SBIC) Program Overview as of September 30, 2015*, accessed September 30, 2016, https://www.sba.gov/sites/default/files/files/WebSBICProgramOverview_September2015.pdf.

Costs of the SBIC Program

Since the beginning of FY2000 (October 1, 1999), the SBA has operated the debenture SBIC program at zero subsidy. The agency accomplishes this by charging the SBICs 3 percent up-front fees and annual fees on the leverage balances. The SBA formulates the annual fees each year, spreading the costs of riskier strategies, such as early-stage investments, across the investment portfolio. As of September 30, 2015, the total amount of private capital and SBA capital at risk in the SBIC program was approximately US\$25.3 billion.¹⁹

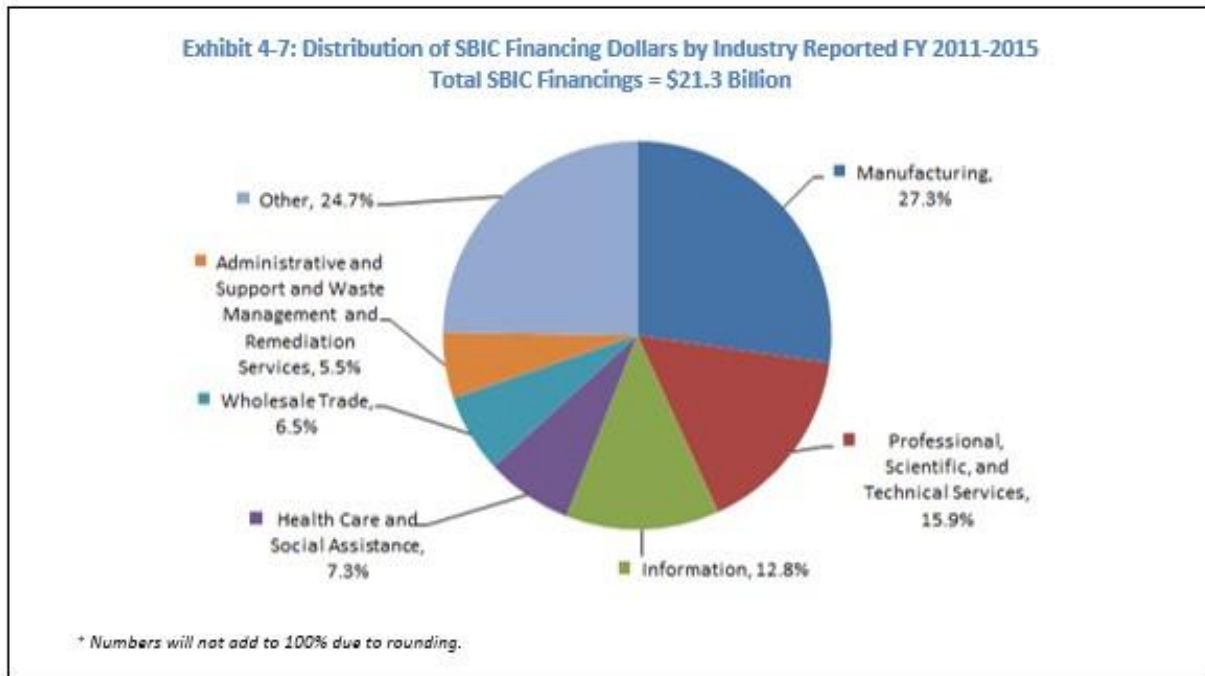
Support for Underserved Industrial Sectors and Geographic Subregions

SBA reporting shows that, from 2011 through 2015, the SBIC program was widely diversified by industry sector, with a high concentration of investments in the manufacturing; professional, scientific, and technical services; and IT sectors (see fig. 2). SBIC investments were likewise varied by geographic subregion, unlike traditional venture capital funding, which is concentrated in large metropolitan areas (see fig. 3).²⁰ In these two aspects—industry sector and geographic subregion distribution—the SBIC program does achieve, as the Urban Institute stated in a 2008 report, the SBA’s goal of “providing capital to entrepreneurs who are underserved by the private venture capital market.”²¹

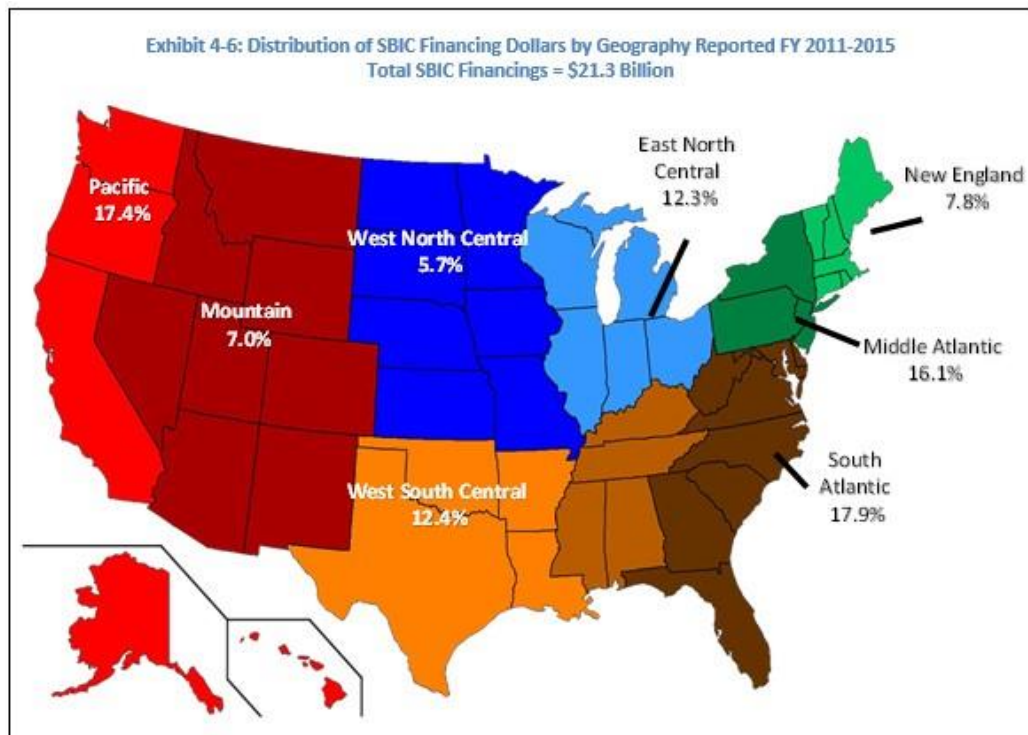
¹⁹ SBA, *Small Business Investment Company (SBIC) Program Overview as of September 30, 2015*.

²⁰ Richard Florida, “A Closer Look at the Geography of Venture Capital in the U.S.,” *CityLab*, February 23, 2016, <http://www.citylab.com/tech/2016/02/the-spiky-geography-of-venture-capital-in-the-us/470208/>.

²¹ Shelli B. Rossman and Brett Theodos, with Rachel Brash et al., *Key Findings from the Evaluation of the Small Business Administration’s Loan and Investment Programs: Executive Summary* (Washington, DC: Urban Institute, 2008), 42, <http://www.urban.org/research/publication/key-findings-evaluation-small-business-administrations-loanand-investment-programs>.

Figure 2. SBIC Financing Distribution by Industry Sector, 2011–15

Source: U.S. Small Business Administration (SBA), *The Small Business Investment Company Program (SBIC): Annual Report; Fiscal Year 2015* (unpublished manuscript, July 13, 2017).

Figure 3. SBIC Financing Distribution by Geographic Subregion, 2011–15

Source: SBA, *The Small Business Investment Company Program (SBIC): Annual Report; Fiscal Year 2015*.

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METHODOLOGY

Data Sources Used to Compare the SBIC Program and Private Equity Universe

For the purposes of this analysis, the authors utilized two sets of proprietary data to define and compare relevant private capital and SBIC investments.

SBIC Proprietary Data. The SBA’s OII, which manages the SBIC program, provided FRD with its data on SBIC fund managers and portfolio companies in which SBIC funds were invested for FY1995–2015. This data was shared “AS IS” with FRD; that is, as it was reported by SBIC managers to the SBA. The SBA makes no representation or warranty, express or implied, with respect to the content, completeness, or accuracy of the information provided.²²

The SBIC data provided by the OII included information collected from SBA Portfolio Financing Report (SBA Form 1031) and SBA Annual Financial Report (SBA Form 468) filings, as well as data in the SBIC company history file. The one-page Portfolio Financing Report contains financial and demographic data on small businesses prior to their receipt of capital support through the SBIC program. The 22-page Annual Financial Report contains annual financials for each SBIC, including employment data on the loans and investments for each year they participate in the program. Schedule 8 of the annual report (SBA Form 468) contains employment and other general data on the portfolio companies. Copies of both forms are provided in appendices III and IV. The complete forms can also be found online at: <https://www.sba.gov/sbic/sbic-resource-library/forms>.

General Investment Data Related to Private Equity Activity in the United States. In order to compare SBIC and non-SBIC fund financings, the authors sought the support of Pitchbook Data, which provides data on the full lifecycle of mergers and acquisitions, private equity, and venture capital transactions, along with information about the entities involved. While Pitchbook provides its data in pre-set options via an online subscription database, the authors acquired core information, allowing for more relevant segmentations and comparisons in relation to the SBIC

²² FRD employees and contractors signed confidentiality agreements that stipulated they would not “publish, divulge, disclose, or make known in any manner” SBIC data.

data received by the SBA. Specifically, the authors requested and received two custom data report files from Pitchbook in November 2016 that included defined data elements related to all funds in their database and to funds of US\$225 million and less, which are more directly comparable to the size limits imposed on SBIC investments.

While the Pitchbook data itself was segmented into 38 individual fund groupings, the authors aggregated the provided data into eight major fund categories with similar characteristics and return-on-investment drivers for analytical purposes. These categories were:

1. **Angel Investors:** Individuals who provide equity investments before businesses start up, seeking to leverage their financial support for a promising idea of product at the earliest stages for a substantial return. *Pitchbook funding categories included:* Angel Investors.
2. **Venture Capital:** Equity investments at different stages of a company lifecycle, usually before any public or broader offering. Venture capitalists typically seek returns by investing in companies with promising, but unproven, revenue or cash-flow streams. *Pitchbook funding categories included:* Venture Capital, Venture Capital–Early Stage, and Venture Capital–Later Stage.
3. **Private Equity Growth–Expansion:** Later-stage investments in companies that, while already generating positive returns, are seeking to expand to the next stage or implement significant changes. *Pitchbook funding categories included:* PE Growth–Expansion.
4. **Private Equity–Buyout:** Equity investments, often coupled with debt financing, aimed at acquiring a majority interest in a company. The inclusion of debt can help investment fund managers enhance their equity returns by inflating internal rates of return on investor capital.²³ *Pitchbook funding categories included:* Buyout.
5. **Debt (non-mezzanine):** Secured or senior debt to companies that assures payback in case of company bankruptcy, either through collateral or because of priority placement in the capital structure. While not as risky as mezzanine debt, investing funds still face risks associated with company bankruptcy or liquidation. *Pitchbook funding categories included:* Bridge Financing, Collateralized Loan Obligation, Credit Special Situations, Debt, Direct Lending, Distressed Debt, Infrastructure, Infrastructure Debt, and Venture Debt.
6. **Mezzanine:** Debt financing to companies which are unsecured and senior only to common shares in the event of a bankruptcy. Because of the higher risk involved, costs

²³ Yolanda Bobeldijk, “The buyout industry’s new trick to boost returns: more debt,” *Financial News*, May 18, 2016, <https://www.fnlondon.com/articles/private-equity-debt-capital-fund-leverage-20160518>.

are usually high and investors have strict performance criteria against which they assess investment potential. *Pitchbook funding categories included:* Mezzanine.

7. **Industry-focused Diversified Funds:** Focused on capital intensive industries, these investments often generate lower rates of return for investors and pose greater risks. *Pitchbook funding categories included:* Energy–Alternative/Renewable, Energy–Oil & Gas, Mining, Real Estate, Real Estate Core, Real Estate Debt, Real Estate Distressed, Real Estate Opportunistic, Real Estate Value Added, and Timber.
8. **Other Funds:** Alternative investment strategies broadening the sources of participation by allowing secondary investors and others to acquire interest in primary investment funds. Many alternative funds serve to explicitly spread the investment risk profile among multiple investors, which can increase investment in areas where debt financing is prohibitively expensive. *Pitchbook funding categories included:* Co-Investment, Diversified Private Equity, Fund of Funds, Hedge Funds, Mezzanine Captive, Project Finance, Restructuring/Turnaround, Secondaries, and Sovereign Wealth Fund.

Data Cohort Used to Size and Explain Capital Markets

For comparison purposes, the authors compiled and analyzed information pertaining to fund attributes, borrower and investee characteristics, and industry sector and geographic subregion representation. The authors identified the following fund size categories for which investment data were populated: all private capital funds, private capital funds less than or equal to US\$225 million (generally the size of the maximum-leveraged SBIC fund), all active SBIC funds, and active debenture only SBIC funds.

The authors applied two universal filters to all categories of funds: 1) investments made between January 1, 2010 and December 31, 2015; and 2) U.S. financings only. January 1, 2010 was selected as the starting point for this analysis given that it was the first complete year after the larger effects of the 2007–8 financial crisis were felt (see table 1).

Table 1. Total Number of Funds and Deals Invested in by Private Capital and SBIC Investors, 2010–15

	Panel A		Panel B	
	All Funds		Funds ≤US\$225M	
Type of Investment	# of Funds	Total # of Deals	# of Funds	Total # of Deals
TOTAL	8,041	35,890	4,105	19,807
Angel Investor	64	855	39	632
Venture Capital	3,617	24,518	2,461	16,757
PE Growth–Expansion	448	2,509	242	1,096
PE–Buyout	1,951	11,395	675	2,723
Debt (non-mezzanine)	391	1,781	100	427
Mezzanine	283	1,795	144	998
Industry-Focused Diversified Funds	569	1,555	160	341
Other Funds	718	2,684	284	1,067
Panel C			SBIC Investments	
Type of Investment			# of Funds	Total # of Deals
All Active SBICs			271	9,037
Active Debenture Only SBICs			192	7,301

It should be noted that in the Pitchbook data, “Total # of Deals” is less than the sum of the individually reported numbers of deals for the eight major investment types for both the “All Funds” and “Funds ≤US\$225M” categories. When more than one fund contributes to a deal, all of the funds get unit credit; therefore, the sums of the deal counts by category exceed the aggregate total numbers of deals reported. For example, if a senior lending fund, mezzanine fund, and private equity group all contribute capital to a deal, each would get credit for participation, resulting in a combined deal count of three; however, the “Total # of Deals” in the aggregate would be just one. Summing all eight major categories for the “All Funds” and “Funds ≤US\$225M” columns yields aggregate deal counts, respectively, of 47,092 (vs. 35,890 reported) and 24,041 (vs. 19,807 reported).

NOTE: REFER TO DISCLAIMER NOTICE

Key Attributes for Comparison

The authors focused their attention on the following characteristics to compare and contrast SBIC debenture funds with similarly situated non-SBIC funds: number of funds, fund size, total number of investments made, investment size, company EBITDA (earnings before interest, tax, depreciation and amortization), company revenues, and investments by fund strategy.

MAIN FINDINGS

Private Equity Universe in the United States

In order to understand the role SBICs play in the broader financing landscape, it is essential to first describe the market for small business financing and investment.

For small businesses, financing and investments typically come from three inter-connected sources: individual investments by business owners or general partners, loans and other debt financing from banks and other institutions and investments—typically for an equity share—by outside investors, both individual and institutional.

Many market participants have observed that in the wake of increased financial regulation following the 2008 financial crisis, many large banks have curtailed their lending to certain types of companies. Small companies have been especially hard hit. A recent study by Harvard University showed that by 2010, overall small business loans had dropped to 60 percent of their 2006 average level. By 2014, they had only returned to 70 percent. The drop was especially large among the nation’s biggest banks.²⁴ The combined lending to small businesses from the top four banks in the United States dropped by more than 50 percent from their 2006 peak, whereas lending from smaller banks fell by much less.²⁵ The pullback in bank lending has created a gap that is beginning to be filled by alternative investment managers who, while once predominantly operating in private equity, now use a variety of alternative lending strategies, many of which rely on new applications of information technology for finance, such as automated business credit scores and peer-to-peer lending.

²⁴ The top four banks in terms of asset size are Bank of America, Citigroup, JPMorgan Chase, and Wells Fargo.

²⁵ Brian S. Chen, Samuel G. Hanson, and Jeremy C. Stein, “The Decline of Big-Bank Lending to Small Business: Dynamic Impacts on Local Credit and Labor Markets” (working paper, Harvard Business School, Harvard University, Boston, Massachusetts, 2017), 1, 38, http://www.people.hbs.edu/shanson/BigBankSmallBiz_paper_20170317_FINAL.pdf.

Ultimately, 8,041 non-SBIC private capital funds invested US\$1.5 trillion into U.S. companies from 2010 through 2015, as shown in panel A of table 2.²⁶ The average fund size across all categories was US\$569.7 million.

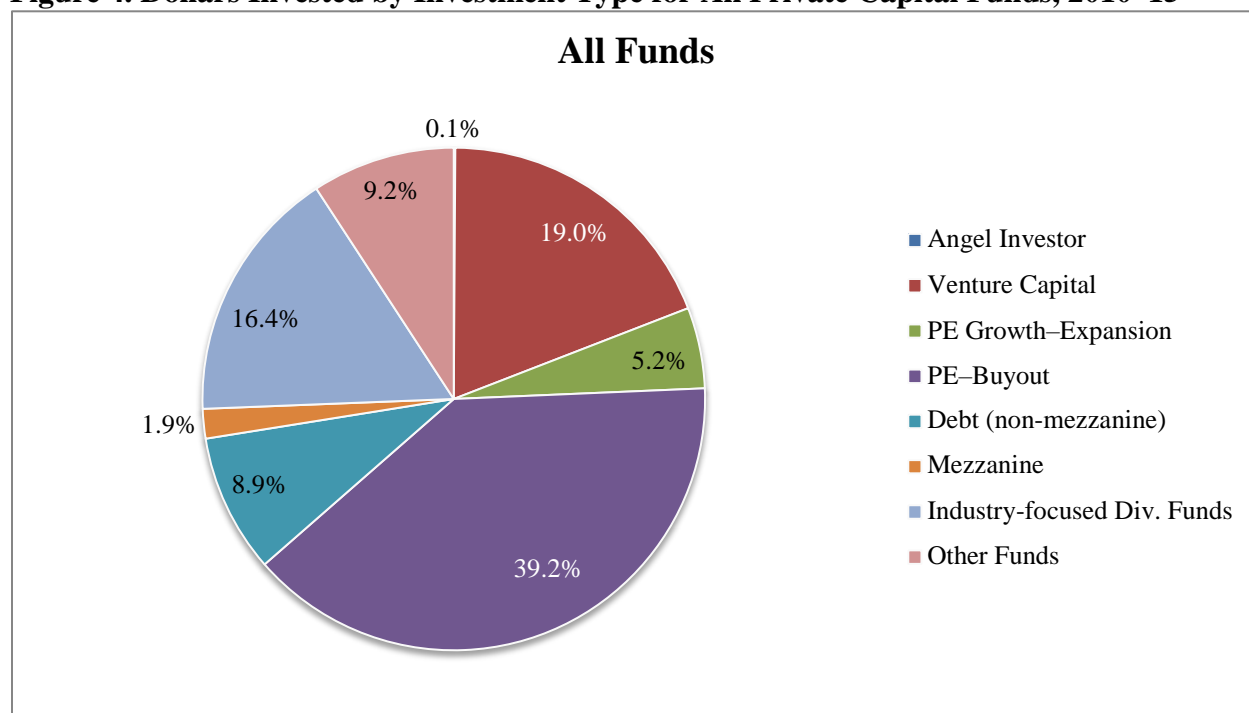
Table 2. Private Capital and SBIC Investments in U.S. Companies, 2010–15

	Total # of Funds	Avg. Fund Size (US\$M)	Total # of Deals	Total Capital Invested (US\$M)	% of All Deals	% of All Capital
Panel A—All Funds						
TOTAL	8,041	569.7	35,890	1,513,386.2	100.0	100.0
Angel Investor	64	10.3	855	3,076.0	1.8	0.1
Venture Capital	3,617	163.1	24,518	390,618.3	52.1	19.0
PE Growth–Expansion	448	332.7	2,509	107,018.9	5.3	5.2
PE–Buyout	1,951	1,061.5	11,395	806,470.9	24.2	39.2
Debt (non-mezzanine)	391	1,095.4	1,781	183,233.4	3.8	8.9
Mezzanine	283	516.2	1,795	38,652.6	3.8	1.9
Industry-focused Diversified Funds	569	1,066.2	1,555	336,662.9	3.3	16.4
Other Funds	718	760.7	2,684	189,122.3	5.7	9.2
Panel B—Funds ≤US\$225M						
TOTAL	4,105	75.7	19,807	335,764.5	100.0	100.0
Angel Investor	39	10.3	632	2,385.7	2.6	0.6
Venture Capital	2,461	65.1	16,757	193,353.9	69.7	47.0
PE Growth–Expansion	242	83.5	1,096	26,666.3	4.6	6.5
PE–Buyout	675	93.1	2,723	48,195.2	11.3	11.7
Debt (non-mezzanine)	100	94.1	427	31,091.8	1.8	7.6
Mezzanine	144	107.4	998	8,968.3	4.2	2.2
Industry-focused Diversified Funds	160	98.1	341	42,443.2	1.4	10.3
Other Funds	284	93.7	1,067	58,495.8	4.4	14.2
Panel C—SBIC Investments						
All Active SBICs	271	77.9	9,037	63,705.0	100.0	100.0
Active Debenture Only SBICs	192	96.3	7,301	58,998.0	100.0	100.0

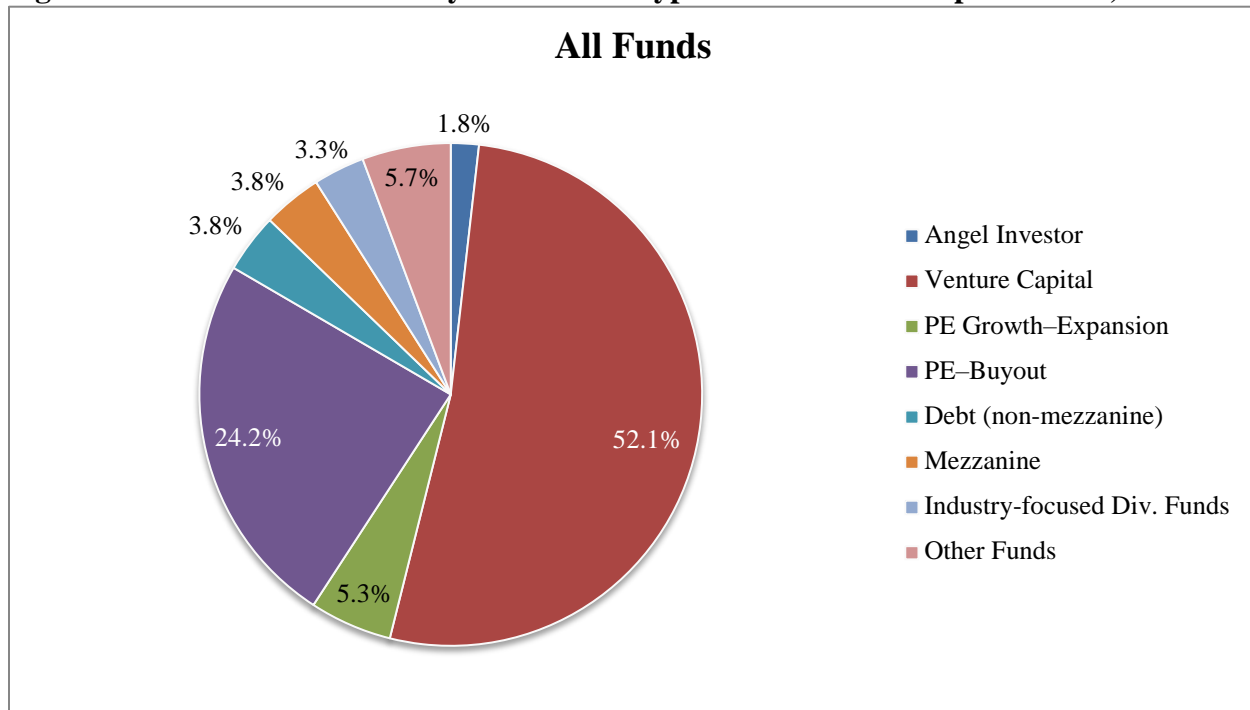
²⁶ Due to the lack of public disclosures for private equity and related funds, it is difficult to directly access or assemble a comprehensive database of relevant information. As noted in the Methodology, for this analysis, the authors relied on custom reports provided by Pitchbook Data.

As discussed in the “Methodology” section, the overall totals for the “Total # of Deals” and “Total Capital Invested” columns in the Pitchbook data are less than the sums of the individually reported numbers of deals for the eight major investment types for both the “All Funds” and “Funds ≤US\$225M” categories.²⁷ The two columns labeled “% of All Deals” and “% of All Capital” account for this by expressing each row as a fraction of the sum totals of the right categories. These columns show, for example, that private equity–buyouts represented almost 40 percent of all capital investments—with US\$806 billion invested—but only about one-quarter of all investments made. As illustrated in figure 4, the total value of private equity–buyout financing was more than twice the next largest investment mechanism, venture capital, which—with US\$390 billion invested—accounted for only 19 percent of all capital investments, even though venture capital accounted for the largest number of transactions (see fig. 5).

Figure 4. Dollars Invested by Investment Type for All Private Capital Funds, 2010–15



²⁷ As previously noted, when more than one fund contributes to a deal, all of the funds get unit credit; therefore, the sums of the deal counts by category exceed the aggregate total numbers of deals reported. For example, if a senior lending fund, mezzanine fund, and private equity group all contribute capital to a deal, each would get credit for participation, resulting in a combined deal count of three; however, the “Total # of Deals” in the aggregate would be just one. Summing all eight major categories for the “All Funds” and “Funds ≤US\$225M” columns yields aggregate deal counts, respectively, of 47,092 (vs. 35,890 reported) and 24,041 (vs. 19,807 reported).

Figure 5. Distribution of Deals by Investment Type for All Private Capital Funds, 2010–15

For funds less than or equal to US\$225 million, however, private equity–buyouts and other fund types play a limited role. This can be seen in figures 6 and 7. The proportions in figure 6 were obtained by scaling the amounts invested by each of the eight major investment categories for funds less than or equal to US\$225 million by the total amount of capital, which is the US\$1.5 billion figure reported at the top of table 2, panel A. As seen in figure 6, venture capital investments for these funds account for 13 percent of all capital.

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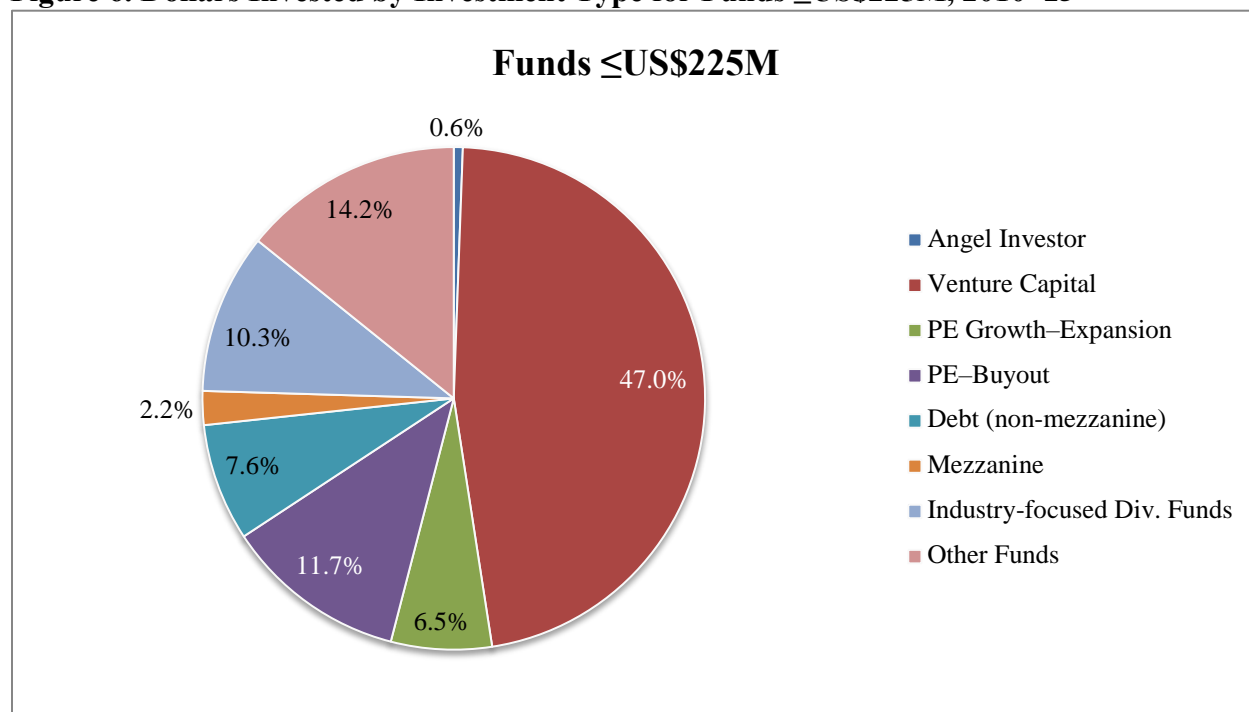
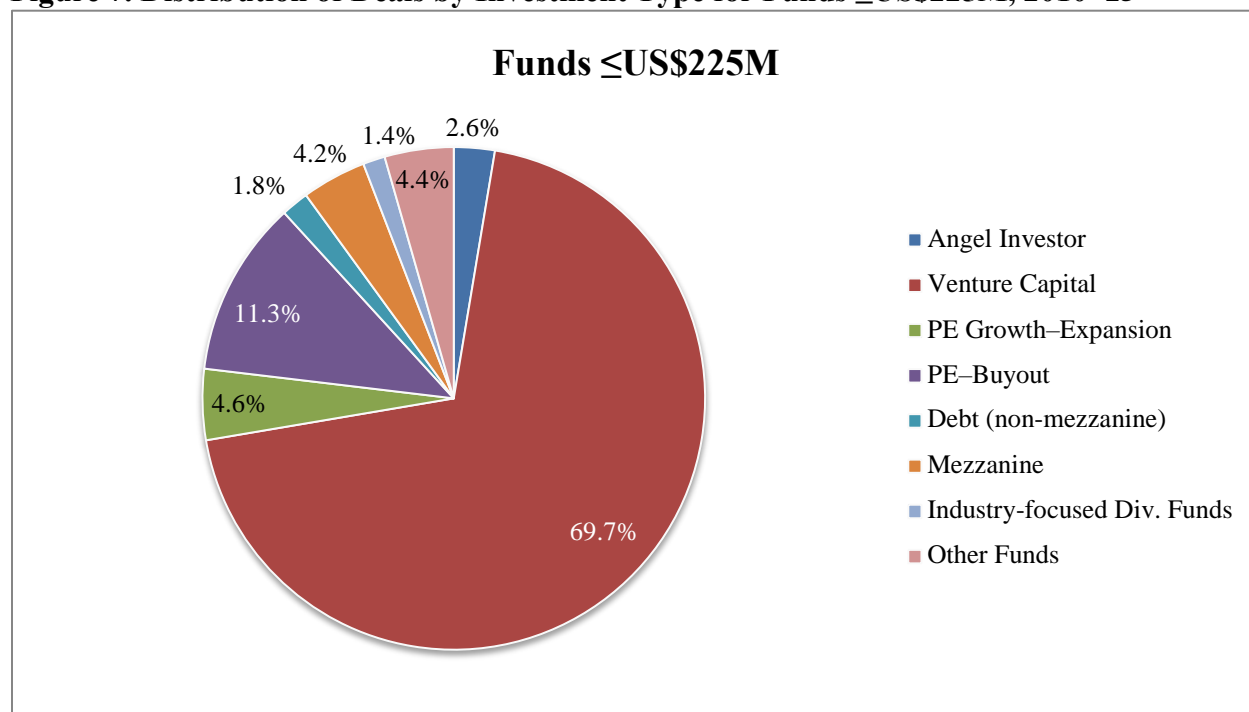
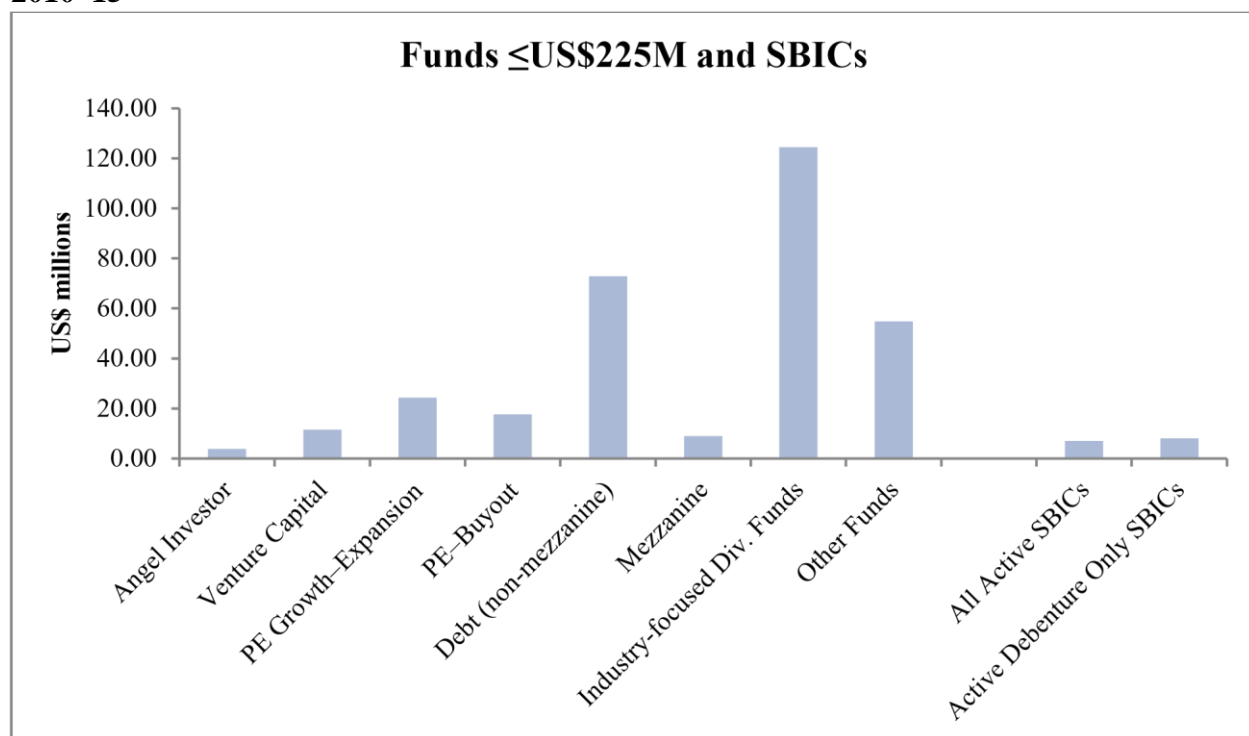
Figure 6. Dollars Invested by Investment Type for Funds ≤US\$225M, 2010–15

Figure 7 expresses the number of investments made by each of the eight major investment categories for funds less than or equal to US\$225 million as a fraction of the total number of investments made by such funds. The fact that venture capital is such a large fraction of the total deal activity, but a relatively smaller fraction of the invested capital, reflects the fact that venture capital investments, like SBIC investments, are much smaller in size than the typical private equity–buyout investment.

This is explored further in figure 8, which reports the capital invested per deal for SBIC funds and for funds less than or equal to US\$225 million. It shows that on a deal-size basis, SBIC funds look similar to angel, venture capital, or mezzanine investors—committing relatively smaller amounts of capital per deal. This highlights the role that SBICs play in the small business market.

Thus, the typical SBIC looks more like a small, growth-oriented private equity or debt (non-mezzanine) firm, both in terms of individual size and in terms of the number of deals and total dollars invested.

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Figure 7. Distribution of Deals by Investment Type for Funds ≤US\$225M, 2010–15**Figure 8. Capital Invested per Deal by Investment Type for Funds ≤US\$225M and SBICs, 2010–15**

NOTE: REFER TO DISCLAIMER NOTICE

Portfolio Company-Level Deal Attributes

To further compare SBIC investments with the broader private equity market, the authors also examined portfolio companies' financial performance as expressed by EBITDA (earnings before interest, tax, depreciation, and amortization) and company revenue. This is contained in table 3.²⁸

Table 3. Portfolio Company-Level Deal Attributes for the U.S. Market, 2010–15

	Avg. Deal Size (US\$M)	Avg. EBITDA (US\$M)	Avg. Revenue (US\$M)	Median Deal Size (US\$M)	Median EBITDA (US\$M)	Median Revenue (US\$M)
Panel A—All Funds						
TOTAL	67.9	159.3	404.3	6.2	(1.4)	22.5
Angel Investor	4.0	47.6	111.8	1.7	(0.9)	2.9
Venture Capital	17.7	61.5	143.9	—	—	—
PE Growth—Expansion	71.9	438.7	522.6	16.0	(2.8)	28.2
PE—Buyout	259.8	119.9	511.4	44.9	13.3	54.7
Debt (non-mezzanine)	194.3	75.5	519.3	—	—	—
Mezzanine	82.1	39.5	148.2	12.0	14.2	36.7
Industry-focused Diversified Funds	430.5	196.6	1,432.5	—	—	—
Other Funds	115.2	65.0	424.7	—	—	—
Panel B—Funds ≤US\$225M						
TOTAL	23.1	36.9	180.5	4.3	(7.7)	12.2
Angel Investor	4.2	—	60.9	1.6	—	2.9
Venture Capital	12.9	(9.4)	54.5	—	—	8.7
PE Growth—Expansion	40.8	9.0	85.9	10.2	(4.7)	18.2
PE—Buyout	69.0	152.3	389.8	14.5	1.3	26.9
Debt (non-mezzanine)	125.9	37.9	456.2	—	—	202.4
Mezzanine	35.9	18.8	93.9	7.5	9.5	28.3
Industry-focused Diversified Funds	257.2	141.7	2,882.2	—	—	598.7
Other Funds	84.7	51.8	282.8	—	—	—
Panel C—SBIC Investments						
All Active SBICs	12.2	3.0	31.6	3.2	2.2	21.4
Active Debenture Only SBICs	13.1	2.9	33.6	4.0	2.2	21.5

²⁸A number of the cells in this table contain missing data. This reflects the fact that it was not possible for the authors to compute the medians for aggregated categories (see pp. 9–10). Also, Pitchbook Data's "Angel Investor" category had very limited data coverage for EBITDA.

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Comparing SBICs to the overall private equity universe, SBICs invest in portfolio companies that are smaller and potentially less profitable on average. This can be seen by comparing the average portfolio company revenues across all private capital funds (US\$404.3 million) to the average for all active SBICs (US\$31.6 million). Even compared to funds less than or equal to US\$225 million, for which average portfolio company revenues are US\$180.5 million, SBIC funds invest in smaller companies.

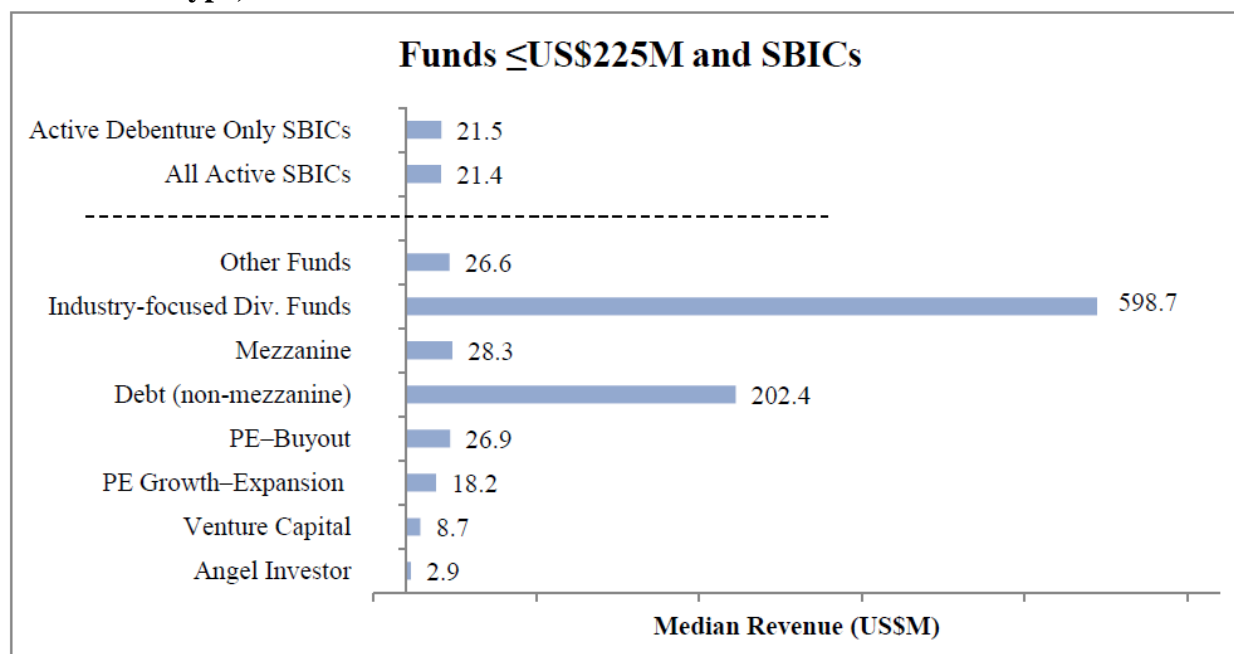
Dividing average EBITDA by average revenue yields a measure of portfolio company average profitability. By this measure, SBIC funds can be seen to invest in less profitable businesses. The average EBITDA/revenue multiple for SBIC-invested portfolio companies is less than 10 percent (3.0/31.6 for all active SBICs and 2.9/33.6 for active debenture only SBICs), whereas the average for all private capital funds (159.3/404.3) is closer to 40 percent, and for funds less than or equal to US\$225 million is 20 percent (36.9/180.5).

However, the average numbers mask substantial skewness in portfolio company characteristics. This can be seen by comparing the median, where available. The fact that SBIC funds and traditional private equity companies are more comparable in terms of median portfolio company characteristics than average characteristics is a reflection of the fact that traditional funds generate much of their success from a small number of highly successful investments. SBIC funds tend to invest in fewer outliers.

At a more granular level, comparing SBICs to individual funds less than or equal to US\$225 million (see fig. 9) shows that the median revenue of companies in which SBICs invest (US\$21.4 million for all active SBICs) are well within the ranges of revenue associated with other “standard” capital investments such as private equity–growth expansion (US\$18.2 million) and private equity–buyouts (US\$26.9 million); only debt funds (US\$202.4 million) and the capital-intensive industry-focused diversified funds (US\$598.7 million) invest in higher revenue companies. As is to be expected, company revenues associated with the early-stage support of angel investors and venture capital investments are much lower (US\$2.9 million and US\$8.7 million, respectively) than other investor categories.

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Figure 9. Median Revenue of Portfolio Companies (Funds ≤US\$225M and SBICs) by Investment Type, 2010–15



PROFILE OF INVESTMENTS BY INDUSTRY SECTOR

Private Capital and SBIC Funding Dollar Distribution by Industry Sector

The authors next considered the industry sector diversification of SBIC program financing and compared it to other similarly sized funds (those less than or equal to US\$225 million), as well as to all other funds investing in the same segment of the marketplace. Pitchbook Data classifies businesses in seven major categories: business-to-business (B2B), business-to-consumer (B2C), energy, financial services, healthcare, information technology (IT), and materials and resources. In order to compare the SBIC and Pitchbook data, the authors obtained a file, called “SIC to PB Industry Mapping,” from Pitchbook in December 2016, and regrouped the SBIC-financed businesses into the seven categories created by Pitchbook.²⁹

Table 4 displays the dollar distribution by industry sector for all private capital funds, those less than or equal to US\$225 million, and SBIC funds.

²⁹ Established in the United States in 1937, the Standard Industrial Classification (SIC) system is used by government agencies to classify industries by a four-digit code.

Table 4. Private Capital and SBIC Funding Dollar Distribution by Industry Sector, 2010–15

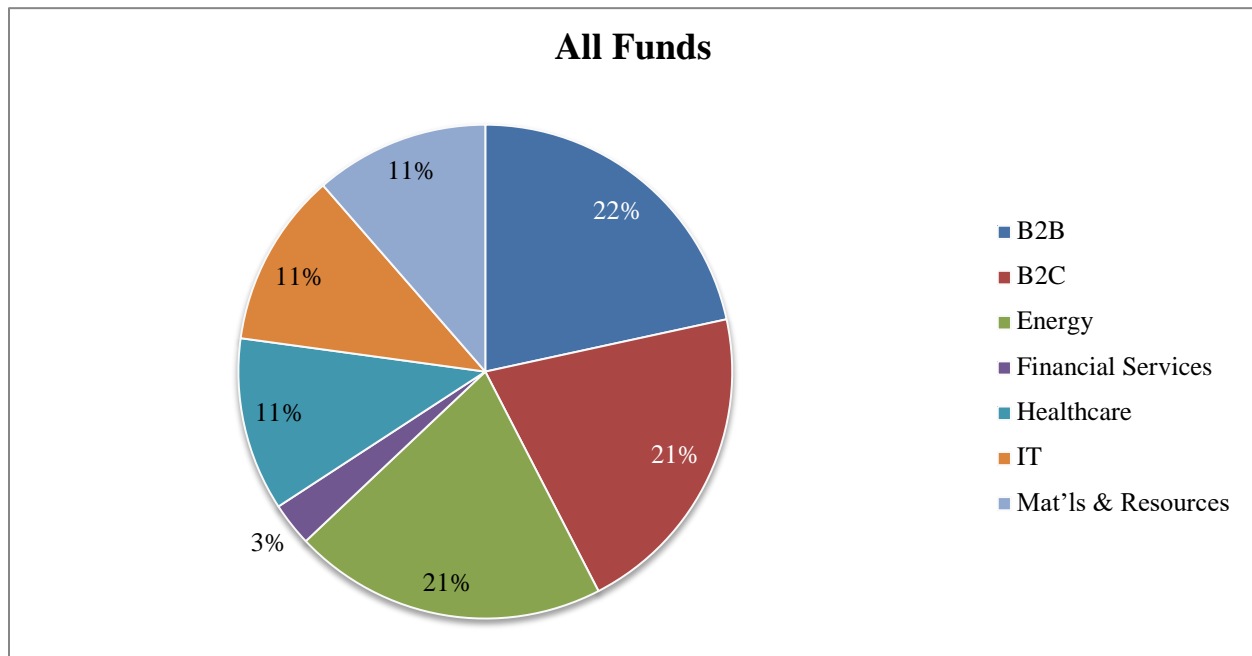
	B2B (US\$B)	B2C (US\$B)	Energy (US\$B)	Financial Services (US\$B)	Healthcare (US\$B)	IT (US\$B)	Mat’ls & Resources (US\$B)
Panel A—All Funds							
TOTAL	326.9	315.1	310.8	43.1	171.9	173.0	172.6
Angel Investor	0.4	0.6	0.0	0.0	0.5	1.5	0.1
Venture Capital	35.8	49.6	27.5	12.5	93.7	168.7	2.8
PE Growth–Expansion	13.9	38.4	7.0	5.7	9.2	30.9	2.0
PE–Buyout	173.2	209.5	44.6	67.7	88.2	193.4	29.9
Debt (non-mezzanine)	46.8	35.9	41.0	19.3	14.2	22.4	3.7
Mezzanine	14.7	4.9	2.0	4.1	4.5	6.9	1.6
Industry-focused Diversified Funds	87.9	51.3	96.5	80.8	1.6	13.8	4.7
Other Funds	25.6	27.7	31.7	24.4	31.2	44.7	3.8
<i>Sector as % of All Funds</i>	<i>21.6</i>	<i>20.8</i>	<i>20.5</i>	<i>2.8</i>	<i>11.4</i>	<i>11.4</i>	<i>11.4</i>
Panel B—Funds ≤US\$225M							
TOTAL	57.6	55.5	31.9	36.0	47.4	105.4	2.0
Angel Investor	0.3	0.4	0.0	0.0	0.3	1.3	0.1
Venture Capital	19.0	24.8	14.9	6.4	42.7	84.2	1.3
PE Growth–Expansion	4.6	10.8	1.1	0.4	2.1	7.2	0.4
PE–Buyout	9.4	6.4	1.9	6.3	4.4	19.3	0.5
Debt (non-mezzanine)	8.2	13.5	2.1	1.1	2.0	4.2	0.0
Mezzanine	1.7	0.8	0.7	3.7	1.4	0.7	0.0
Industry-focused Diversified Funds	11.7	9.0	4.4	12.5	0.1	4.7	0.0
Other Funds	9.9	5.9	10.5	8.9	5.5	17.5	0.2
<i>Sector as % of All Funds</i>	<i>17.2</i>	<i>16.5</i>	<i>9.5</i>	<i>10.7</i>	<i>14.1</i>	<i>31.4</i>	<i>0.6</i>
Panel C—SBIC Investments							
All Active SBICs	8.7	1.6	0.1	0.8	1.6	6.2	0.9
Active Debenture Only SBICs	8.2	1.5	0.1	0.8	1.5	5.8	0.9
<i>Sector as % of All Active SBICs</i>	<i>43.7</i>	<i>8.2</i>	<i>0.5</i>	<i>4.1</i>	<i>7.9</i>	<i>31.0</i>	<i>4.6</i>
<i>Sector as % of Active Debenture Only SBICs</i>	<i>43.5</i>	<i>8.2</i>	<i>0.5</i>	<i>4.1</i>	<i>8.2</i>	<i>30.8</i>	<i>4.7</i>

Private Capital Funding Dollar Distribution (All Funds) by Industry Sector

As shown in panel A of table 4, for all private capital funds, the largest concentration of capital went into B2B (US\$327 billion), followed by B2C (US\$315 billion) and energy (US\$311 billion). Together, these three sectors accounted for almost two-thirds (63 percent) of all funds (see fig. 10).

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Figure 10. Private Capital Funding Dollar Distribution (All Funds) by Industry Sector, 2010–15



As might be expected in such complex segmentation, there is no apparent correlation between the investment-type composition of any industry-sector funding and the distribution of funds across all seven sectors. For example, as illustrated in figures 11 and 12, the fund category with the largest investment into B2B was private equity–buyout (US\$173.2 billion, or 22 percent of sector funding). However, overall private equity–buyout invested the most into B2C (US\$209.5 billion, or 26 percent of funds). Similarly, venture capital invested more in healthcare than other fund types (US\$93.7 billion, or 54 percent of sector funding), but invested its largest contribution into IT (US\$168.7 billion, or 44 percent of funds).

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Figure 11. Private Capital Funding Dollar Distribution (All Funds) by Industry Sector and Investment Type, 2010–15

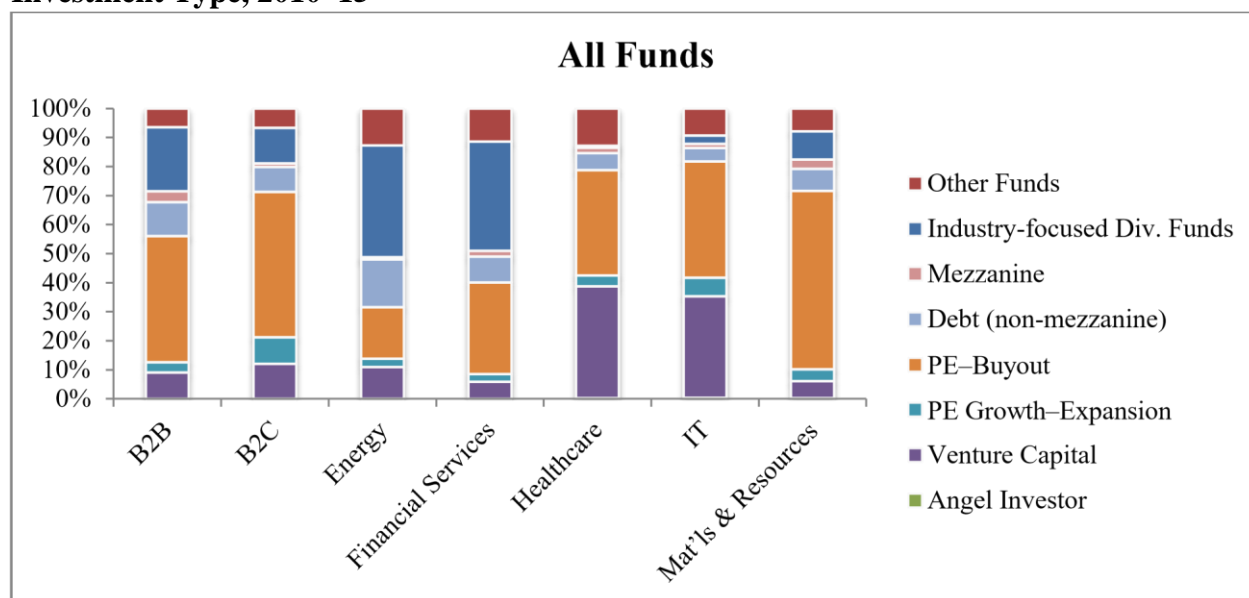
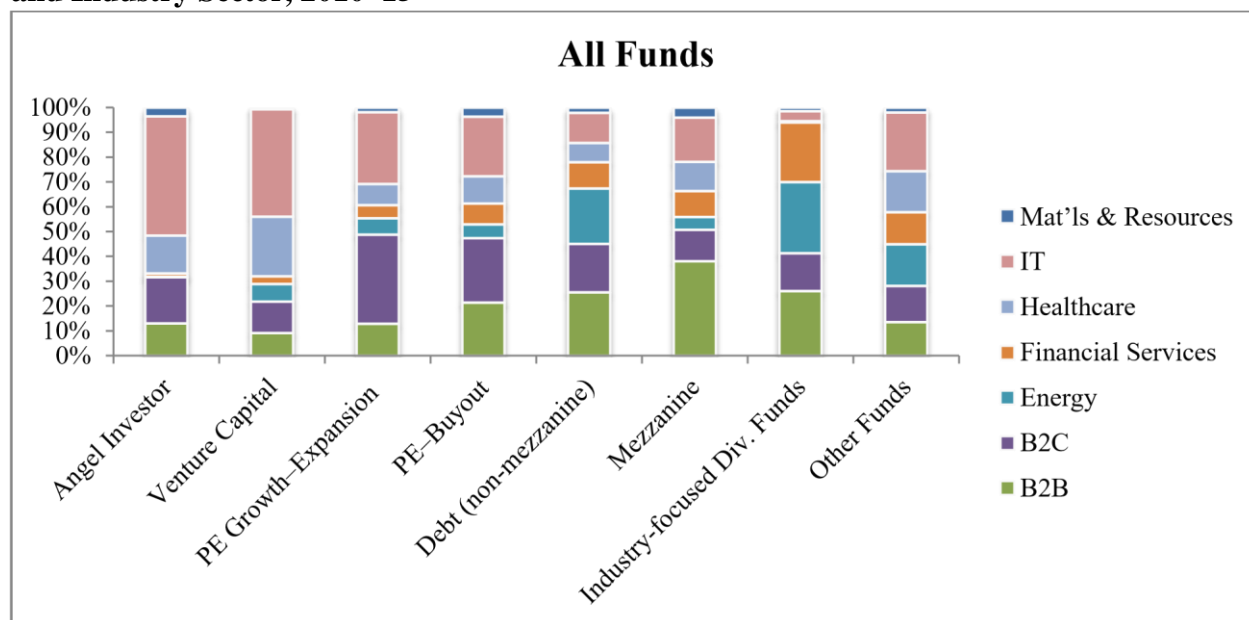


Figure 12. Private Capital Funding Dollar Distribution (All Funds) by Investment Type and Industry Sector, 2010–15

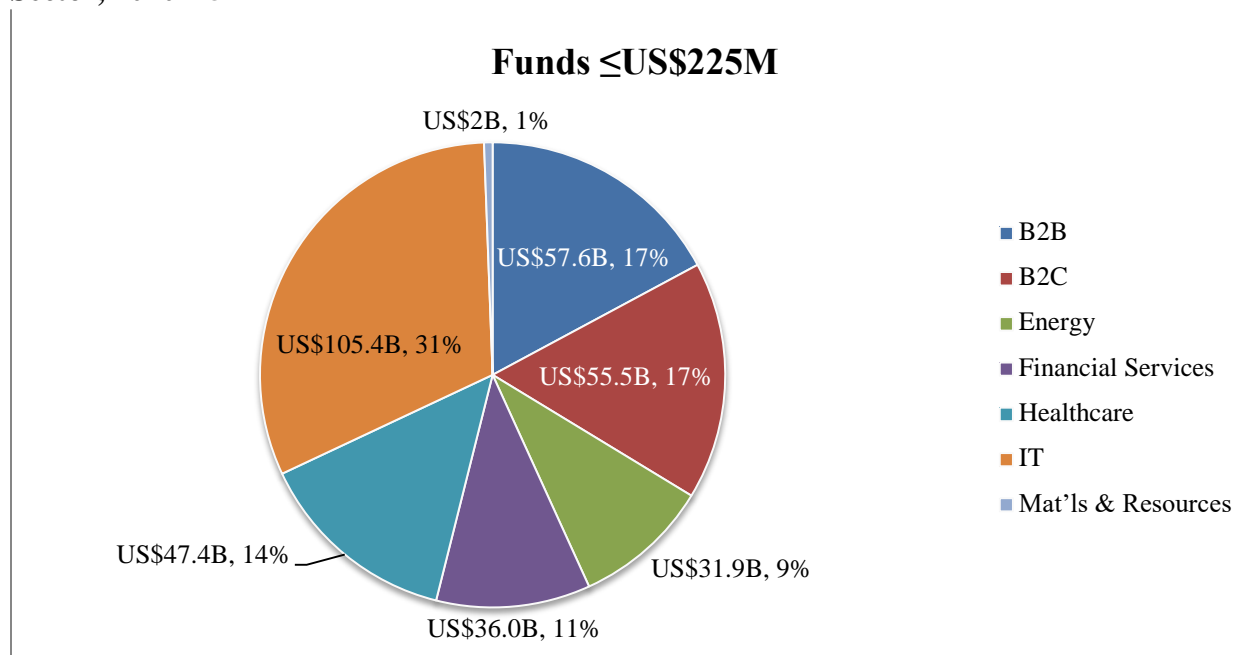


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Private Capital Funding Dollar Distribution (Funds \leq US\$225M) by Industry Sector

Compared to the “All Funds” category’s emphasis on the B2B, B2C, and energy sectors, funds less than or equal to US\$225 million invested the most in the IT sector (US\$105.4 billion, or 31 percent of funds), followed by the B2B and B2C sectors (US\$57.6 billion and US\$55.5 billion, respectively), as shown in figure 13.

Figure 13. Private Capital Funding Dollar Distribution (Funds \leq US\$225M) by Industry Sector, 2010–15



As is the case with the larger “All Funds” category, investment patterns for funds less than or equal to US\$225 million are complex (see fig. 14 and 15). For example, venture capital investments comprised the greatest portion of healthcare funding (US\$43 billion, or 55 percent of sector funding), while contributing the most funds to IT (US\$84 billion, or 44 percent of funds).

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Figure 14. Private Capital Funding Dollar Distribution (Funds ≤US\$225M) by Industry Sector and Investment Type, 2010–15

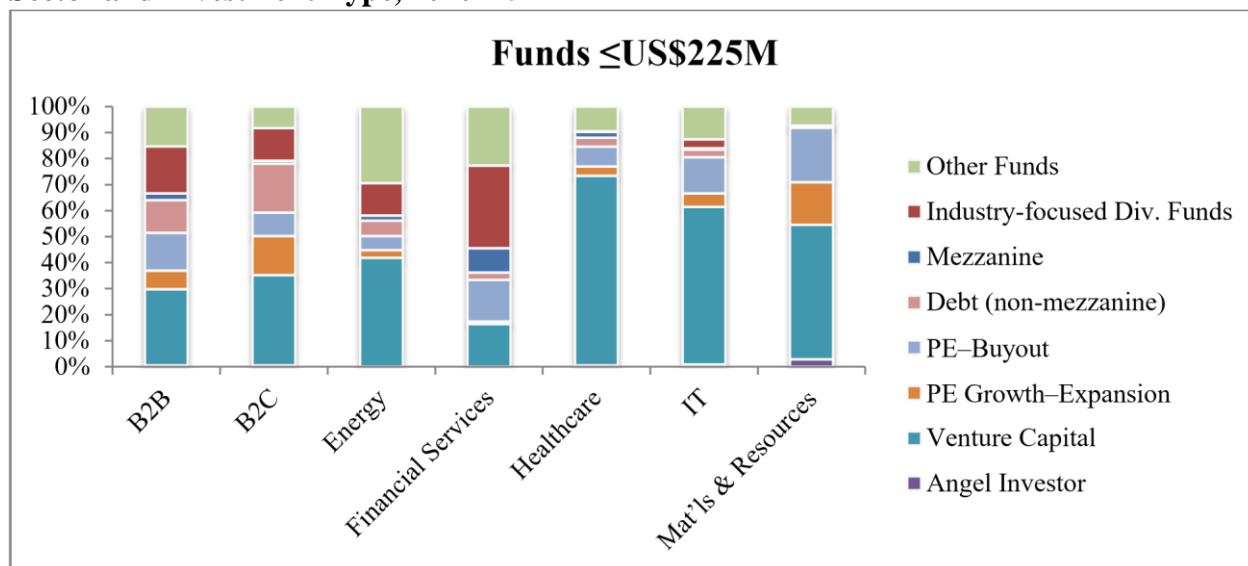
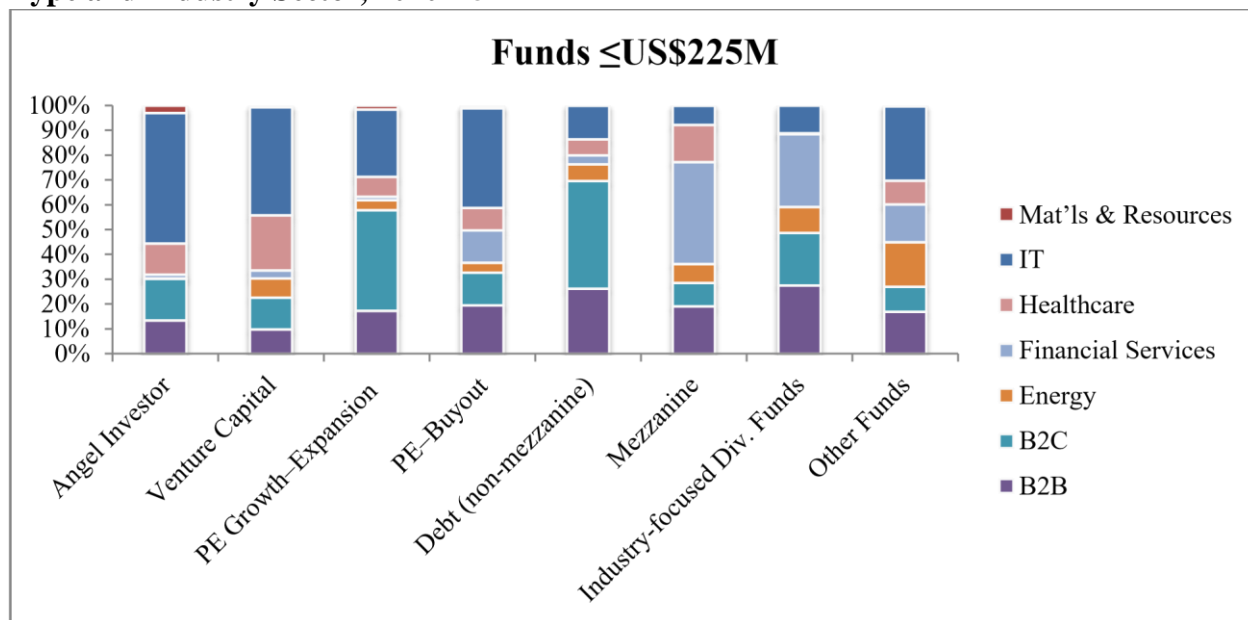


Figure 15. Private Capital Funding Dollar Distribution (Funds ≤US\$225M) by Investment Type and Industry Sector, 2010–15

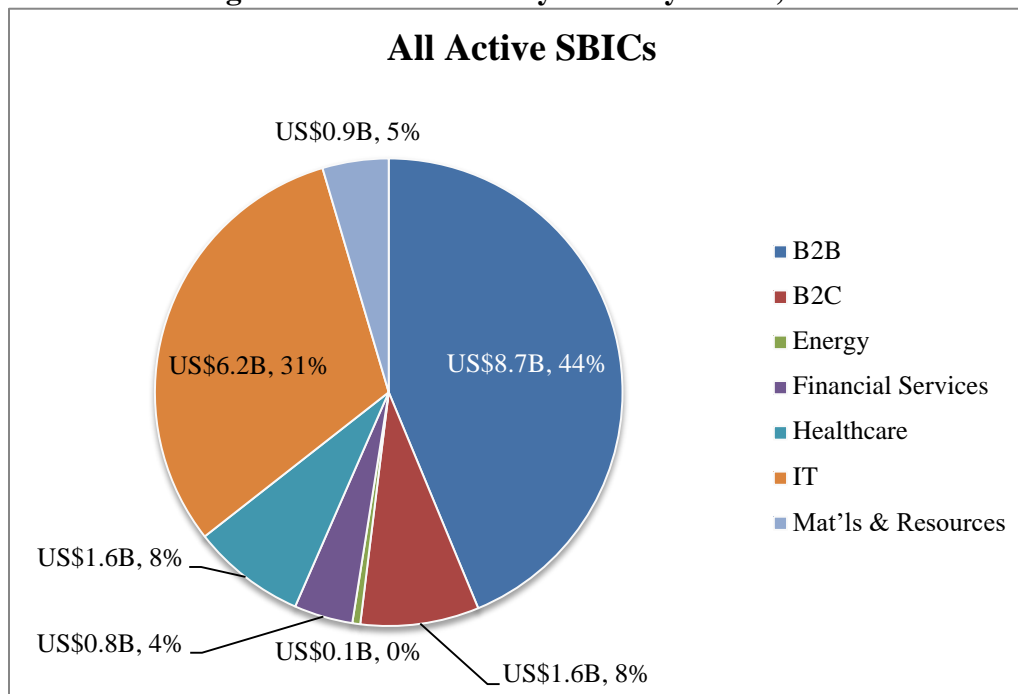


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Comparing Private Capital and SBIC Funding Dollar Distribution by Industry Sector

SBIC funding is much more concentrated than the investments made by private capital funds, with 75 percent of all SBIC funds invested in B2B (US\$9 billion, or 44 percent) and IT (US\$6 billion, or 31 percent) (see fig. 16).³⁰

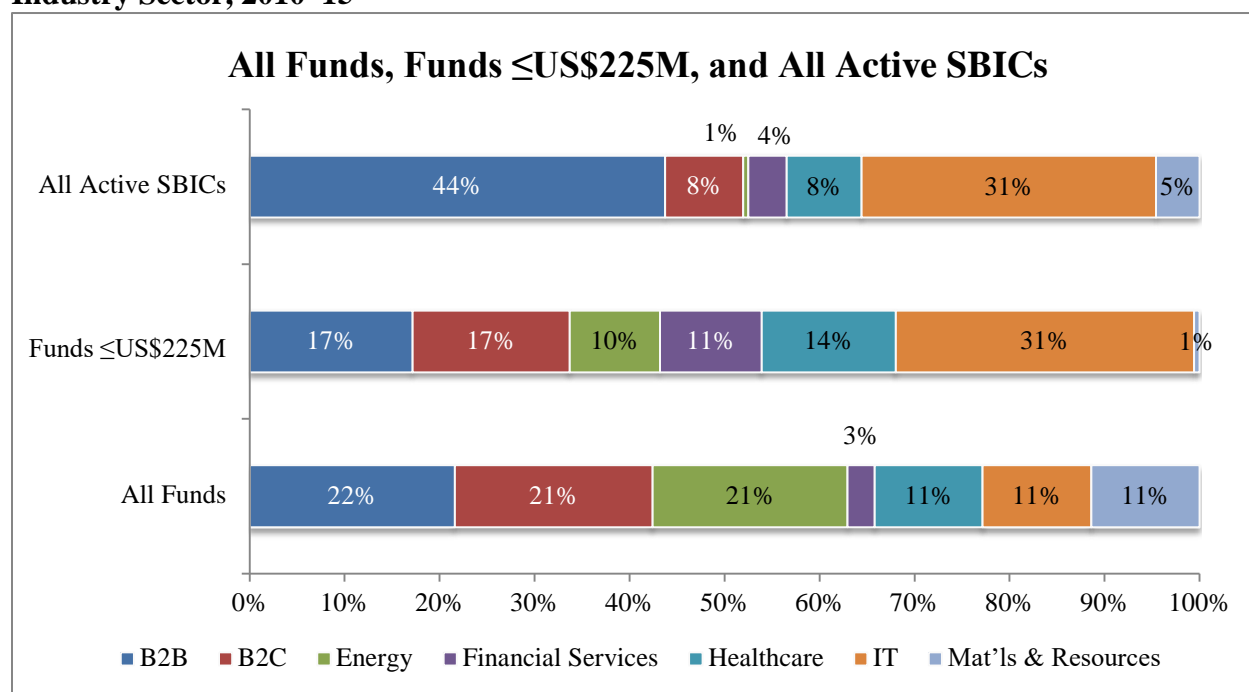
Figure 16. SBIC Funding Dollar Distribution by Industry Sector, 2010–15



A comparison of industry sector investments by funding category (see fig. 17) shows very few similarities across all private capital and SBIC funds. Overall, all private capital funds are more evenly distributed than funds less than or equal to US\$225 million or SBIC funding, with two clear groupings of sector participation: B2B, B2C, and energy equally account for almost two-thirds of the funds, while healthcare, IT, and materials and resources equally account for the remaining third. In contrast, the investment distribution for funds less than or equal to US\$225 million and all active SBICs is much more fragmented.

³⁰ The distribution of “All Active SBIC” and “Active Debenture Only SBIC” funding is virtually identical with only nominal differences on sector contribution (less than 0.3 percent variance). As a result, the analysis looks only to all active SBICs.

Figure 17. Comparison of Private Capital and SBIC Funding Dollar Distribution by Industry Sector, 2010–15



In terms of relative share, SBIC funding by industry sector is only similar to the overall investment percentage for funds less than or equal to US\$225 million in IT (31 percent for all active funds). However, SBICs deployed their largest concentration of dollars toward B2B (43.7 percent for all active funds), which is considerably higher than the 22 percent invested for all funds. SBICs also invested considerably less in B2C (8.2 percent vs. 16.5 percent), energy (0.5 percent vs. 9.5 percent), and healthcare (8.2 percent vs. 14.1 percent) than funds less than or equal to US\$225 million.

Private Capital and SBIC Funding Deal Distribution by Industry Sector

Table 5 details the numbers of deals provided by the various fund categories by sector.

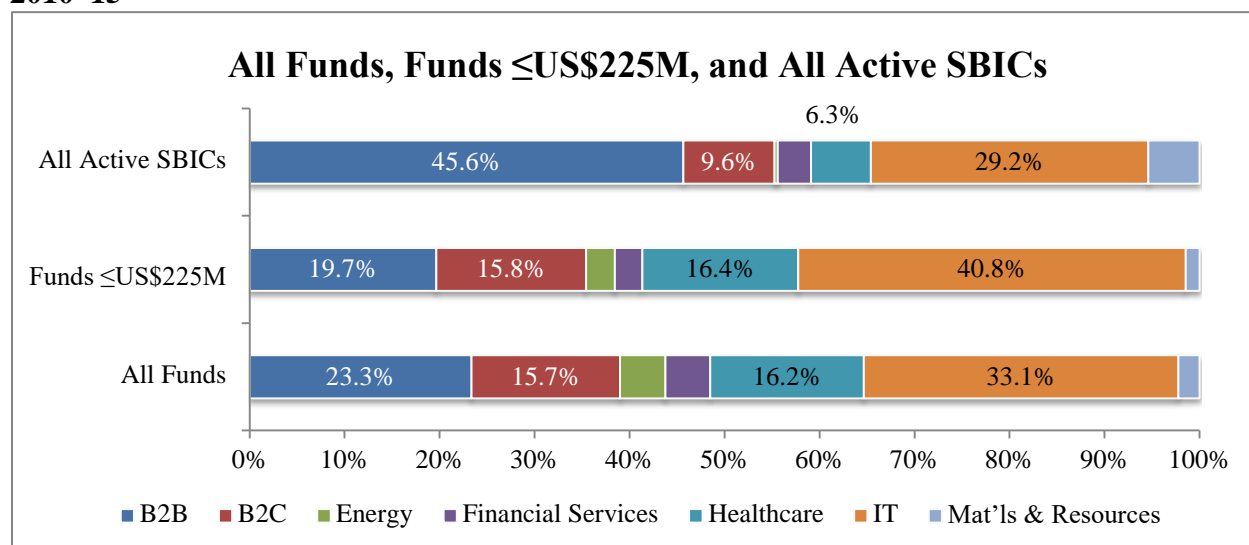
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Table 5. Private Capital and SBIC Funding Deal Distribution by Industry Sector, 2010–15

	B2B	B2C	Energy	Financial Services	Healthcare	IT	Mat'l's & Resources
Panel A—All Funds							
TOTAL	8,377	5,620	1,716	1,695	5,798	11,889	795
Angel Investor	127	133	6	14	122	441	12
Venture Capital	3,107	3,529	587	495	4,353	12,234	430
PE Growth–Expansion	596	402	97	136	383	854	125
PE–Buyout	4,070	2,014	473	992	1,709	1,685	858
Debt (non-mezzanine)	491	257	257	156	171	402	89
Mezzanine	792	347	54	41	274	229	97
Industry-focused Diversified Funds	620	179	498	100	46	84	73
Other Funds	560	360	131	217	562	771	185
<i>Sector as % of All Funds</i>	<i>23.3</i>	<i>15.7</i>	<i>4.8</i>	<i>4.7</i>	<i>16.2</i>	<i>33.1</i>	<i>2.2</i>
Panel B—Funds ≤US\$225M							
TOTAL	3,894	3,120	603	574	3,248	8,080	288
Angel Investor	102	90	3	13	78	338	8
Venture Capital	2,186	2,613	380	325	2,701	8,401	151
PE Growth–Expansion	278	178	30	45	171	375	19
PE–Buyout	1,104	490	117	161	397	349	105
Debt (non-mezzanine)	124	67	36	28	44	122	6
Mezzanine	438	181	22	22	145	163	27
Industry-focused Diversified Funds	175	47	63	14	9	33	0
Other Funds	219	158	51	66	236	320	17
<i>Sector as % of All Funds</i>	<i>19.7</i>	<i>15.8</i>	<i>3.0</i>	<i>2.9</i>	<i>16.4</i>	<i>40.8</i>	<i>1.5</i>
Panel C—SBIC Investments							
All Active SBICs	4,074	858	29	315	562	2,607	481
Active Debenture Only SBICs	3,395	758	25	252	536	1,769	465
<i>Sector as % of All Active SBICs</i>	<i>45.6</i>	<i>9.6</i>	<i>0.3</i>	<i>3.5</i>	<i>6.3</i>	<i>29.2</i>	<i>5.4</i>
<i>Sector as % of Active Debenture Only SBICs</i>	<i>47.2</i>	<i>10.5</i>	<i>0.3</i>	<i>3.5</i>	<i>7.4</i>	<i>24.6</i>	<i>6.5</i>

As shown in figure 18, most of the deals invested by non-SBIC funds were in the IT field (33.1 percent), followed by the B2B (23.3 percent), healthcare (16.2 percent) and B2C (15.7 percent) sectors. In contrast, SBIC funds were lower in IT relative to the broader industry and higher in B2B, B2C, energy, and healthcare.

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Figure 18. Comparison of Private Capital and SBIC Deal Distribution by Industry Sector, 2010–15

Looking closely at individual fund types again demonstrates the diversity in funding across industry sectors. Once again, angel investors and venture capital funds show similar patterns of behavior across all sectors, but other commonalities are harder to discern. Angel investors and venture capital funds in particular invested heavily in the IT sector whereas private equity–buyout funds had the highest investment concentration in B2B deals.³¹ SBICs had a much higher number of B2B deals than IT deals, with B2B accounting for nearly 75 percent of all deals; sectors with high capital requirements, like energy and healthcare, were much less covered by SBICs.

From the tables and figures above it is clear that there are pronounced differences between SBICs and their traditional private capital counterparts in terms of their industry coverage. SBICs tend to invest more in service-oriented businesses where capital requirements are lower. Compared to private capital investors, SBICs tend to fund safer businesses, where there is commensurately less risk and less need for follow-on investments. This is a natural consequence of the tilt in their investment strategy towards debt and debt-like investments.

³¹ The IT category for venture capital exceeds the “All Funds” counts due to multiple funds participating in one deal.

PROFILE OF INVESTMENTS BY GEOGRAPHIC SUBREGION

After reviewing the funding distribution of private capital and SBIC investments by industry sector, the authors examined the breakdown of dollars and deals by geographic subregion.

Pitchbook Data provided the authors with data on investments by state. The authors then aggregated the state-level data into four major regions based on U.S. Census Bureau mapping: Northeast, Midwest, South, and West. Each of these four regions was further divided into two or three subregions (see table 6).

Table 6. U.S. Census Bureau’s Four Major Regions and Nine Subregions of the United States

Region/Subregion	States Included*	Business Population
Northeast		
Middle Atlantic (MA)	NJ, NY, PA	882,840
New England (NE)	CT, MA, ME, NH, RI, VT	317,528
Midwest		
East North Central (ENC)	IL, IN, MI, OH, WI	828,659
West North Central (WNC)	IA, KS, MN, MO, NE, ND, SD	443,537
South		
East South Central (ESC)	AL, KY, MS, TN	282,716
South Atlantic (SA)	DC, DE, FL, GA, MD, NC, SC, VA, WV	1,165,969
West South Central (WSC)	AR, LA, OK, TX	623,954
West		
Mountain (M)	AZ, CO, ID, MT, NM, NV, UT, WY	465,595
Pacific (P)	AK, CA, HI, OR, WA	1,002,787

* *Authors’ Note:* The SBA also provides financing to small businesses in U.S. territories, such as Puerto Rico, but those figures are not included in this analysis.

Source: U.S. Census Bureau, *Census Regions and Divisions of the United States*, accessed December 5, 2016, http://www2.census.gov/geo/pdfs/maps-data/maps/reference/us_regdiv.pdf.

Additionally, the authors used U.S. Census Bureau statistics for U.S. businesses from 2014 to obtain a count of the number of firms in each state. Collectively, as of December 2014, there were approximately 5.8 million businesses in the United States.³² The authors then combined these figures with the Pitchbook data to calculate two capital penetration ratios according to geographic subregion: dollars per business and businesses per deal.

³² U.S. Census Bureau, “2014 SUSB Annual Data Tables by Establishment Industry: U.S. & states, totals,” December 2016, <https://www.census.gov/data/tables/2014/econ/susb/2014-susb-annual.html>.

They calculated dollars per business by dividing the amount of “All Funds” deals (in dollars) per subregion by the number of businesses in each subregion. The authors then computed the number of businesses per deal by dividing the business population of a subregion by the number of “All Funds” deals for that subregion.

Private Capital and SBIC Funding Dollar Distribution by Geographic Subregion

Table 7 provides a deeper look at the results reported in table 6 by examining the subregional distribution of funding dollars for all funds, funds less than or equal to US\$225 million, and SBIC funds.

Table 7. Private Capital and SBIC Funding Dollar Distribution by Geographic Subregion, 2010–15

		Panel A		Panel B		Panel C			
		All Funds		Funds ≤US\$225M		SBIC Investments			
						All Active SBICs		Active Debenture Only	
Region/ Subregion	Bus. Pop.	Dollars (US\$M)	Dollars per Bus. (US\$M)	Dollars (US\$M)	Dollars per Bus. (US\$M)	Dollars (US\$M)	Dollars per Bus. (US\$M)	Dollars (US\$M)	Dollars per Bus. (US\$M)
Northeast									
MA	882,840	248,913	281,946	44,676	50,605	2,990	3,387	2,792	3,163
NE	317,528	107,291	337,895	29,142	91,778	1,530	4,818	1,421	4,475
Midwest									
ENC	828,659	224,350	270,739	32,059	38,688	2,472	2,983	2,353	2,840
WNC	443,537	45,685	103,002	5,425	12,231	1,221	2,753	1,157	2,609
South									
ESC	282,716	29,255	103,478	2,702	9,557	704	2,490	655	2,317
SA	1,165,969	218,192	187,134	43,763	37,534	3,738	3,206	3,535	3,032
WSC	623,954	225,043	360,672	33,154	53,135	2,577	4,130	2,474	3,965
West									
M	465,595	98,108	210,715	21,039	45,187	1,428	3,067	1,286	2,762
P	1,002,787	302,833	301,991	123,321	122,978	3,603	3,593	3,417	3,408

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For all private capital funds, the largest amount of funding dollars (US\$302.8 billion) were in the Pacific subregion, followed by the Middle Atlantic subregion (US\$248.9 billion). The East South Central subregion was the lowest (US\$29.3 billion).

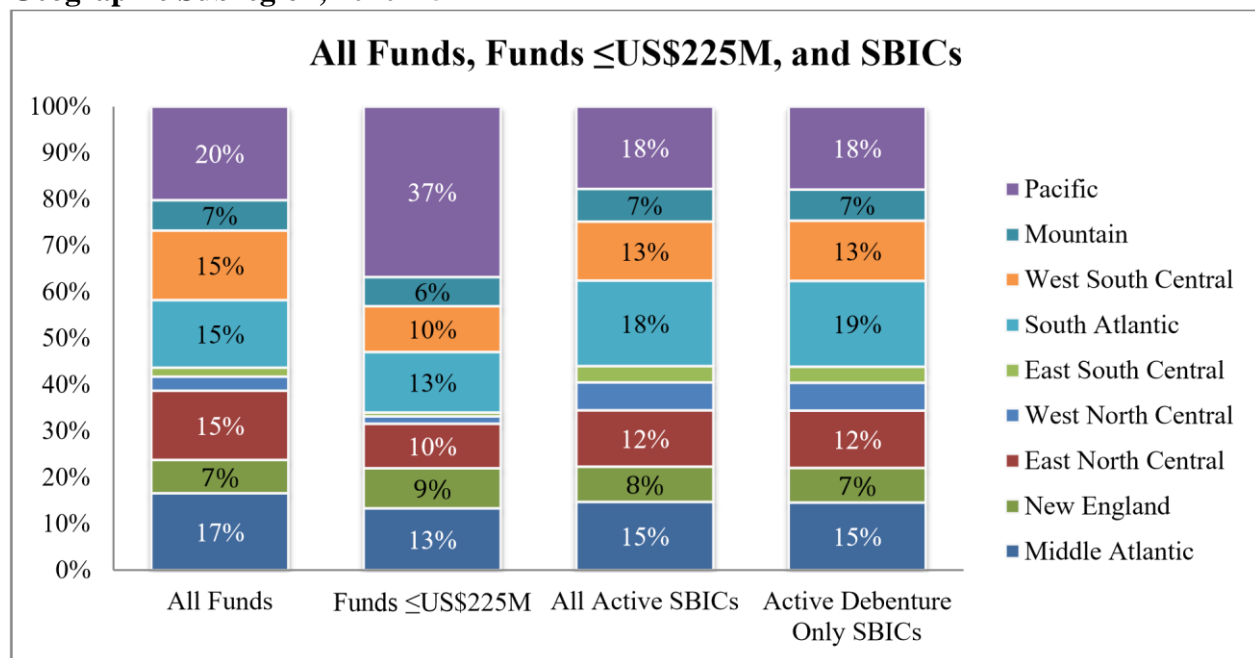
For funds less than or equal to US\$225 million, a similar pattern is evident, with the Pacific subregion accounting for the largest amount of funding dollars (US\$123.3 billion), followed by the Middle Atlantic subregion (US\$44.7 billion); the East South Central and West North Central subregions received the lowest amount of funds (US\$2.7 billion and US\$5.4 billion, respectively).

For both all active and active debenture only SBICs, the largest amount of funding dollars were in the South Atlantic subregion (US\$3.7 billion and US\$3.5 billion, respectively). The East South Central subregion received the lowest amount (less than US\$1 billion for both types of SBIC funds).

A comparison of the geographic distribution of investments across all private capital funds, funds less than or equal to US\$225 million, and SBICs (see fig. 19) highlights both notable differences and similarities:

- While all private capital deals are significantly concentrated in the Pacific subregion, this was much more the case for funds less than or equal to US\$225 million, where 37 percent of funds were invested, compared to 20 percent for all private capital funds.
- In contrast, SBIC financings were much more evenly distributed, with roughly equal amounts in both the South Atlantic and Pacific subregions, followed closely by the Middle Atlantic and West South Central subregions.

Figure 19. Comparison of Private Capital and SBIC Funding Dollar Distribution by Geographic Subregion, 2010–15



Private Capital and SBIC Funding Dollars per Business Ratio

Another way of looking at the deal distribution of private capital and SBIC funding is by standardizing the number of dollars per subregion by the population of businesses (dividing dollars by number of businesses) in that subregion (see table 8).

Table 8. Detailed View on Private Capital and SBIC Funding Dollar Distribution by Geographic Subregion, 2010–15

Type of Investment	Region/Subregion								
	Northeast		Midwest		South			West	
	MA	NE	ENC	WNC	ESC	SA	WSC	M	P
Business Populations	882,840	317,528	828,659	443,537	282,716	1,165,969	623,954	465,595	1,002,787
Panel A—All Funds									
Angel Investor	497	135	270	10	195	88	57	130	1,692
Venture Capital	43,160	48,652	14,749	4,855	2,238	30,715	23,838	26,073	196,337
PE Growth–Expansion	12,771	6,248	9,750	2,602	2,666	19,360	17,700	15,371	19,775
PE–Buyout	131,557	39,261	144,276	32,538	23,082	139,271	115,142	58,083	119,592
Debt (non-mezzanine)	29,377	18,717	24,394	4,436	2,233	32,042	31,017	9,220	30,461
Mezzanine	1,484	2,076	13,210	1,133	395	5,812	3,561	3,013	7,964
Industry-focused Diversified Funds	60,783	20,733	47,366	4,059	1,075	37,879	83,367	23,498	49,541
Other Funds	40,506	23,316	12,269	2,425	3,099	25,161	33,078	4,124	45,099
<i>All Funds</i>	<i>248,913</i>	<i>107,291</i>	<i>224,350</i>	<i>45,685</i>	<i>29,255</i>	<i>218,192</i>	<i>225,043</i>	<i>98,108</i>	<i>302,833</i>
<i>All Funds as % of Total</i>	<i>16.6</i>	<i>7.2</i>	<i>15.0</i>	<i>3.0</i>	<i>2.0</i>	<i>14.5</i>	<i>15.0</i>	<i>6.5</i>	<i>20.2</i>
Dollars per Business	281,946	337,895	270,739	103,002	103,478	187,134	360,672	210,715	301,991
Panel B—Funds ≤US\$225M									
Angel Investor	395	58	247	3	147	78	18	84	1,355
Venture Capital	24,450	16,969	9,794	2,273	972	17,499	11,743	7,999	101,653
PE Growth–Expansion	1,622	924	2,452	492	138	1,713	2,934	9,564	6,686
PE–Buyout	3,725	3,761	6,046	641	741	5,842	3,777	1,746	21,843
Debt (non-mezzanine)	6,400	478	2,010	952	39	8,222	2,047	449	10,496
Mezzanine	885	444	1,086	200	84	1,314	377	323	4,255
Industry-focused Diversified Funds	6,275	5,602	8,637	263	908	10,908	4,330	2,211	3,038
Other Funds	9,722	5,768	4,848	1,324	152	9,832	10,724	1,370	14,755
<i>All Funds</i>	<i>44,676</i>	<i>29,142</i>	<i>32,059</i>	<i>5,425</i>	<i>2,702</i>	<i>43,763</i>	<i>33,154</i>	<i>21,039</i>	<i>123,321</i>
<i>All Funds as % of Total</i>	<i>13.3</i>	<i>8.7</i>	<i>9.6</i>	<i>1.6</i>	<i>0.8</i>	<i>13.1</i>	<i>9.9</i>	<i>6.3</i>	<i>36.8</i>
Dollars per Business	50,605	91,778	38,688	12,231	9,557	37,534	53,135	45,187	122,978
Panel C—SBIC Investments									
All Active SBICs	2,990	1,530	2,472	1,221	704	3,738	2,577	1,428	3,603
Active Debenture Only SBICs	2,792	1,421	2,353	1,157	655	3,535	2,474	1,286	3,417
<i>All Active SBICs as % of Total</i>	<i>14.8</i>	<i>7.6</i>	<i>12.2</i>	<i>6.0</i>	<i>3.5</i>	<i>18.4</i>	<i>12.7</i>	<i>7.0</i>	<i>17.8</i>
<i>Active Debenture Only SBICs as % of Total</i>	<i>14.6</i>	<i>7.4</i>	<i>12.3</i>	<i>6.1</i>	<i>3.4</i>	<i>18.5</i>	<i>13.0</i>	<i>6.7</i>	<i>17.9</i>

For all private capital funds, when standardizing the results by business population, the West South Central subregion had the highest ratio of US\$360,672 funded dollars per business, followed by the New England subregion at US\$337,895. The lowest ratios fell to the East South

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Central and West North Central subregions, each with slightly more than US\$103,000 funded dollars per business.

For funds less than or equal to US\$225 million, the best ratio of dollars to businesses was in the Pacific subregion (US\$122,978), followed by the New England subregion (US\$91,778). The lowest ratios were, once again, in the East South Central and West North Central subregions (less than US\$15,000 funded dollars per business).

Applying the same dollars per business ratio to SBIC funding, the highest ratio was in the New England subregion at US\$4,818 for all active SBICs and US\$4,475 for active debenture only SBICs. This was followed closely by the West South Central subregion. See table 7.

Private Capital and SBIC Funding Deal Distribution by Geographic Subregion

Table 9 shows the subregional deal distribution for all private capital funds, funds less than or equal to US\$225 million, and SBIC funds.

Table 9. Private Capital and SBIC Funding Deal Distribution by Geographic Subregion, 2010–15

		Panel A		Panel B		Panel C			
		All Funds		Funds ≤US\$225M		SBIC Investments			
		# of Deals	# of Bus. per Deal	# of Deals	# of Bus. per Deal	All Active SBICs		Active Debenture Only	
Region/ Subregion	Bus. Pop.					# of Deals	# of Bus. per Deal	# of Deals	# of Bus. per Deal
Northeast									
MA	882,840	5,283	167	2,985	296	1,384	638	1,034	854
NE	317,528	3,129	101	1,791	177	674	471	546	582
Midwest									
ENC	828,659	3,552	233	1,807	459	1,015	816	861	962
WNC	443,537	1,229	361	582	762	533	832	435	1,020
South									
ESC	282,716	945	299	460	615	299	946	245	1,154
SA	1,165,969	4,357	268	1,958	595	1,754	665	1,519	768
WSC	623,954	3,167	197	1,276	489	1,136	549	1,042	599
West									
M	465,595	1,989	234	1,032	451	799	583	483	964
P	1,002,787	12,133	83	7,872	127	1,437	698	1,130	887

As shown in panel A of table 9, the largest overall deal count by far for all private capital funds was in the Pacific subregion (12,133). The second largest deal concentration was in the Middle Atlantic subregion (5,283), which had less than half as many deals as the Pacific. The lowest number of deal counts was recorded in the East South Central subregion (945).

Private capital funds less than or equal to US\$225 million show a similar pattern, with the greatest number of deals by far in the Pacific subregion (7,872), followed by the Middle Atlantic subregion (2,985), which had less than one-third the number of deals in the Pacific subregion. Deals were the lowest in the East South Central subregion (460).

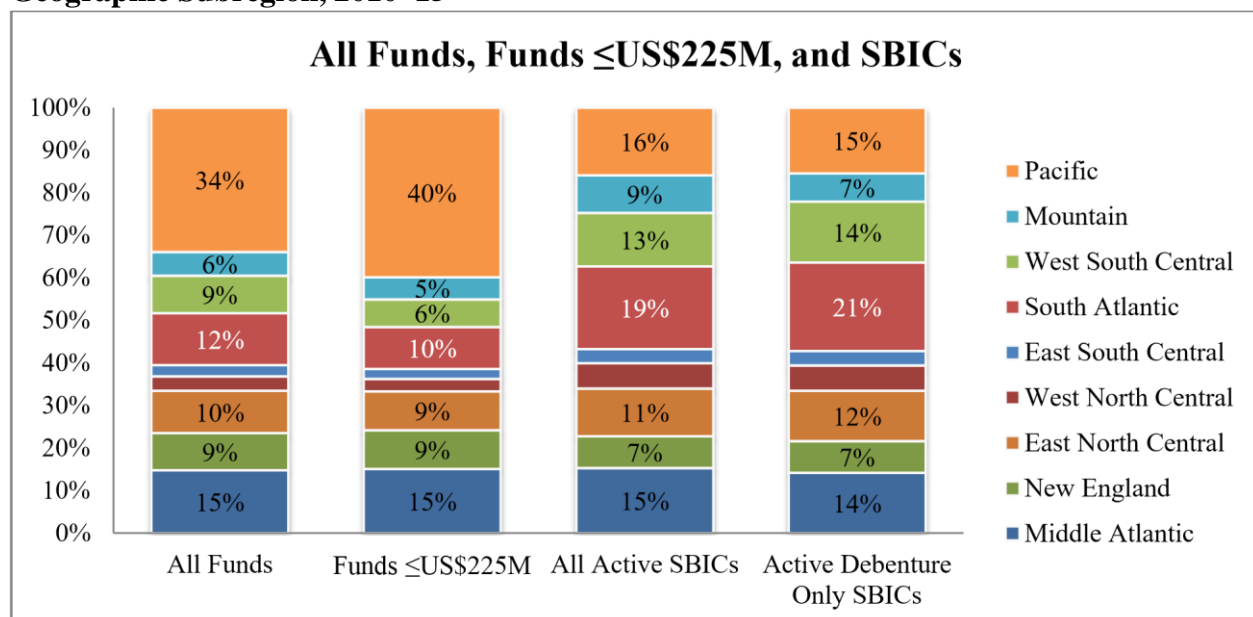
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Among SBICs, the greatest number of deals was found in the South Atlantic subregion (3,273), followed closely by the Pacific (2,567), Middle Atlantic (2,418), and West South Central (2,178) subregions. As with the private capital funds, the East South Central subregion received the least number of SBIC deals (544).

A comparison of the distribution and concentration of funding deals, as shown in figure 20, highlights both notable differences and similarities between all private capital funds, funds less than or equal to US\$225 million, and SBICs:

- All private capital deals are significantly concentrated in the Pacific subregion, and then in the Middle Atlantic subregion, accounting for 50 percent or more of all deals.
- In contrast, SBIC financing events are most concentrated in the South Atlantic subregion, which represents almost one-fifth of all deals. However, SBIC deals in the Pacific and Middle Atlantic subregions play a close second and third.
- The East South Central and West North Central subregions are the least likely locations for deals of any type.

Figure 20. Comparison of Private Capital and SBIC Funding Deal Distribution by Geographic Subregion, 2010–15

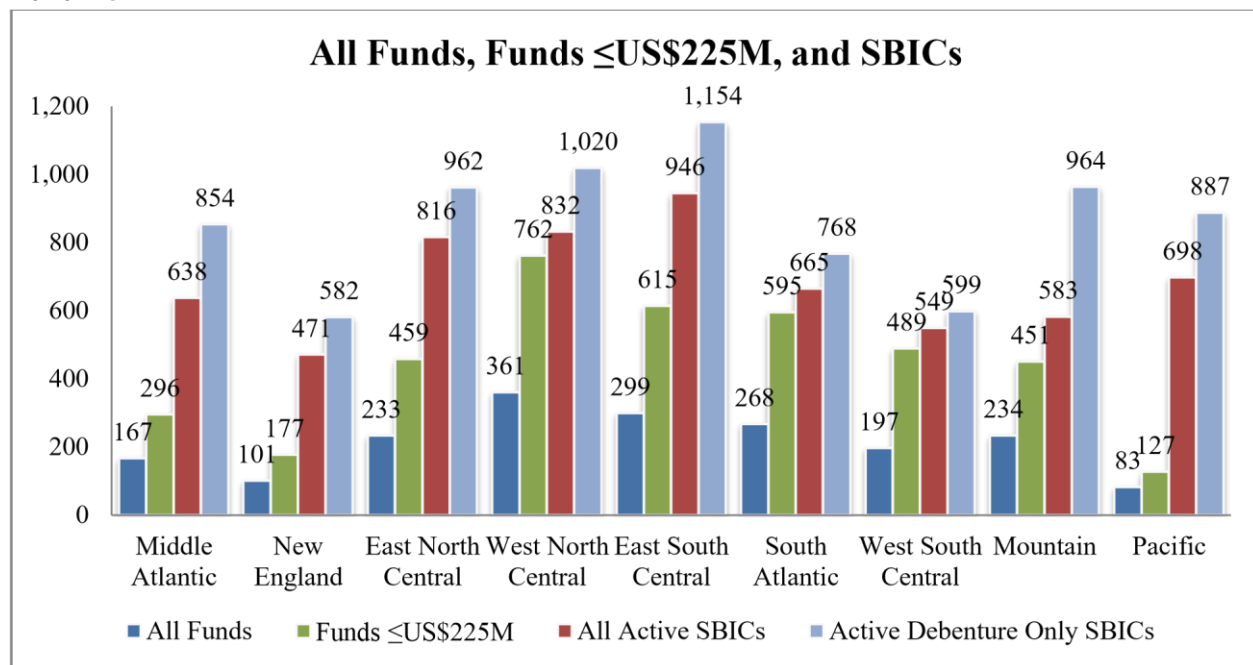


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Businesses per Private Capital and SBIC Funding Deal Distribution Ratio

The ratio of businesses per number of deals provides a convenient measure to standardize a comparison of funding across the nine subregions by providing a per capita view of how many businesses, on average, received capital funding. A lower ratio suggests a greater availability of funding within the subregion (see fig. 21).

Figure 21. Businesses per Private Capital and SBIC Funding Deal Distribution Ratio, 2010–15



When standardizing the data by the number of business entities, the varying impacts of capital funding across the subregions becomes more apparent:

- For non-SBIC private capital funding, the Pacific subregion has the lowest business population per deal ratio (83 for all private capital funds and 127 for funds less than or equal to US\$225 million), mirroring the subregion’s importance in terms of the absolute number of deals and the relative concentration of investment. Stated differently, one out of every 83 businesses, on average, received some level of capital funding. In contrast, the least favorable ratios in the West North Central subregion varied by almost a factor of five, with one out every 361 businesses, on average, receiving some level of capital funding, and one out of every 762 businesses, on average, receiving investments from funds less than or equal to US\$225 million.

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- For SBICs, the lowest businesses per deal ratio was found in the New England subregion (471 for all active SBICs, 582 for active debentures only SBICs) despite the relative low volume of deals in the subregion. Unlike the dramatic variance seen with private capital funds, however, the SBIC ratios were more moderate—the least favorable ratio (found in the East South Central subregion) differs from the best ratio by a factor of two or less.

Based on this data, SBICs reflect a broader and more consistent geographic presence than private capital funds on all three counts measured: total number of deals, relative concentration across subregions, and business population per deal ratio.

When compared to the subregional data for dollar distribution, it appears that SBICs spread capital in a more geographically dispersed manner. There is far less concentration of SBIC funding on the West Coast than for all private capital funds. Indeed, much more of it goes to emerging markets (traditionally underserved markets, such as women, minorities, and veterans).

RESEARCH NOTES

It is important to mention a few caveats for the findings. First, the data on funds, deals, and investee businesses are not complete. What the authors have analyzed and presented in this report represent the best and most complete data available on the financings and investments for small and mid-sized businesses. In some instances, it is difficult to draw absolute distinctions between the SBIC data and the broader private equity universe due to incomplete data and differing definitions of variables. The authors have identified these inconsistencies to, potentially, allow the reader to draw different conclusions. Despite these data issues, the authors conclude that investments by SBICs are more heavily concentrated in industries and communities where traditional private equity investment activity has been lacking.

It is also important to note that the authors' ability to determine whether SBICs add tangible or intangible value not otherwise provided by non-SBIC private equity funds depended greatly on the availability of non-SBIC fund data that were of a similar level of detail and granularity as the information provided by the SBA. Given the inherently private nature of such data, the authors were unable to draw sharp conclusions here.

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CONCLUSION

Congress created the SBIC program in the 1950s, at a time when the private equity industry in its current form did not exist. Indeed, in some sense the program itself was the very catalyst behind the development of the U.S. private equity industry as we know it today.³³ In the years since the passage of the Small Business Investment Act, private equity has grown to a US\$1 trillion dollar industry; subindustries have evolved that focus private equity at firms of all shapes and sizes. It is important to ask in the context of this changing market what role the SBIC program plays in the broader private equity market.

The goal of this report is to contribute to a deeper understanding of the role that the SBIC program has played in providing financing and investment to the small business sector. Focusing on the time period from 2010 through 2015, the authors analyzed 9,037 total SBIC financings and compared them to the broader financing environment for small and mid-sized businesses. The findings from this exercise indicate that SBIC-funded small businesses are a robust source of capital and investment in the U.S. economy.

Several main themes emerge from the analysis. The first is that SBIC funds focus capital on firms that might not otherwise appear attractive to private equity investors. The average firm receiving SBIC capital is smaller in size and less profitable than the average private equitybacked firm. The investments of SBICs look most like those of small, growth-capital or debtoriented private equity companies.

A second theme concerns the distribution of investments and investment capital across industries. SBIC funds contributed capital in all seven major industrial sectors during the sample period. The B2B and IT sectors showed the most activity across both the overall small and midsize funds by a large margin.

The third theme concerns geographic patterns in investment activity. SBIC investment capital is spread much more evenly across the United States; much less is concentrated in the traditional hubs of private equity investment activity like the Pacific subregion, which is home to Silicon

³³ George W. Fenn, Nellie Liang, and Stephen Prowse, “The Private Equity Market: An Overview,” *Financial Markets, Institutions, and Instruments* 6, no. 4 (1997): 11.

Valley. The authors' analysis of the geographic dispersion of investments revealed that SBIC funds contributed capital in all four geographic regions and nine subregions of the United States.

The data are less clear cut on whether portfolio companies receive greater intangible benefits from the SBICs than they might receive from traditional private equity concerns. However, in previous reports prepared by the authors for the OII—*Measuring the Representation of Women and Minorities in the SBIC Program* (October 2016) and *Measuring the Role of the SBIC Program in Small Business Job Creation* (January 2017)—they found that the SBIC program stimulates business activity among the women- and minority-led business communities, and that it is an important source of capital for facilitating job creation for small businesses.³⁴ These findings alone suggest that there may be important intangible value not otherwise provided by non-SBIC private equity funds.

To supplement these findings, the authors conducted interviews with several investors in SBICs. Many stated that the ability to operate larger capital bases by relying on SBA leverage attracted more talented fund managers than would otherwise have been possible, had the funds been operating at a smaller scale. In light of the fact that academic research has shown that an important source of intangible value that private equity investors provide for their portfolio companies is the business advice they offer, one way to interpret the qualitative evidence the authors collected is that the SBIC program may facilitate the flow of better quality information into this market than would otherwise be available by attracting more talented investors.

All told, the tangible and intangible evidence on SBICs suggests that they continue to play an important role in the private equity landscape. They continue to play a role in diversifying access to private capital some sixty years after their creation jumpstarted the private equity industry as we know it today.

³⁴ Paglia and Robinson, *Measuring the Representation of Women and Minorities in the SBIC Program*; Paglia and Robinson, *Measuring the Role of the SBIC Program in Small Business Job Creation*.

APPENDIX I. GLOSSARY

Angel Investors

Individuals who provide equity investments before businesses start up, seeking to leverage their financial support for a promising idea of product at the earliest stages for a substantial return.

Business-to-Business (B2B)

A situation where one business makes a commercial transaction with another. This typically occurs when: a business is sourcing materials for their production process (e.g. a food manufacturer purchasing salt); a business needs the services of another for operational reasons (e.g. a food manufacturer employing an accountancy firm to audit their finances); or a business re-sells goods and services produced by others (e.g. a retailer buying the end product from the food manufacturer).

Business-to-Consumer (B2C)

A business or transactions conducted directly between a company and consumers who are the end-users of its products or services.

Community Reinvestment Act

Enacted by Congress in 1977, the Community Reinvestment Act is intended to encourage depository institutions to help meet the credit needs of the communities in which they operate.

Debenture

A corporate finance term that refers to a medium- to long-term debt instrument used by large companies to borrow money at a fixed rate of interest. For the purposes of the Small Business Investment Company (SBIC) program, while authorized under the Small Business Investment Act to have a maximum term of 15 years, substantially all SBIC debentures are issued for a 10-year term.

Debt (non-mezzanine)

Secured or senior debt to companies that assures payback in case of company bankruptcy, either through collateral or because of priority placement in the capital structure. While not as risky as mezzanine debt, investing funds still face risks associated with company bankruptcy or liquidation.

Debt Financing

Financing based on debt instruments, such as bond issues or long-term notes payable.

NOTE: REFER TO DISCLAIMER NOTICE

Debt-Plus-Equity Financing

Financing based on debt instruments, such as bond issues or long-term notes payable, and equity, such as common stocks, preferred stocks, or retained earnings.

Dodd-Frank Wall Street Reform and Consumer Protection Act

Signed into law by President Barack Obama on July 21, 2010, this act is intended to promote the financial stability of the United States by improving accountability and transparency in the financial system, to protect American taxpayers by ending bailouts, and to protect consumers from abusive financial services practices, among other purposes.

Equity Capital/Financing

Money raised by a business in exchange for an ownership share of the company, by either owning shares of stock outright or having the right to convert other financial instruments into stock. Two key sources of equity capital for new and emerging businesses are angel investors and venture capital firms.

Industry-focused Diversified Funds

Focused on capital intensive industries, these investments often generate lower rates of return for investors and pose greater risks.

Hybrid Financing

Combined debt and equity financing.

Leverage

The ratio of a company's loan capital (debt) to the value of its common stock (equity).

Licensee

A private investment fund licensed as an SBIC by the U.S. Small Business Administration (SBA).

Limited Partnership

A partnership consisting of a general partner, who manages the business and generally has unlimited liability for the business's debts and obligations, and a limited partner, who has limited liability but cannot participate in the management of the business.

Lower-Middle Market

The market segment containing businesses with between US\$5 million and US\$100 million in annual revenues.

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Mezzanine Financing

Mezzanine debt is used by companies that are cash-flow positive to fund further growth through expansion projects, acquisitions, recapitalizations, and management and leveraged buyouts. When mezzanine debt is used in conjunction with senior debt, it reduces the amount of equity required in the business. As equity is the most expensive form of capital, it is most cost effective to create a capital structure that secures the most funding, offers the lowest cost of capital, and maximizes return on equity.

North American Industry Classification System (NAICS)

The standard used by federal statistical agencies in classifying business establishments for the purpose of collecting, analyzing, and publishing statistical data related to the U.S. economy.

Office of Investment and Innovation (OII)

The office within the SBA that operates the SBIC Program.

Other Funds

Alternative investment strategies broadening the sources of participation by allowing secondary investors and others to acquire interest in primary investment funds. Many alternative funds serve to explicitly spread the investment risk profile among multiple investors, which can increase investment in areas where debt financing is prohibitively expensive.

Portfolio Company

An entity in which a venture capital firm, buyout firm, holding company, or other investment fund invests. All of the companies currently backed by a private equity firm can be referred to as the firm's portfolio.

Private Equity/Capital

An asset class consisting of equity securities and debt in operating companies that are not publicly traded on a stock exchange. A private equity investment will generally be made by a private equity firm, a venture capital firm, or an angel investor.

Private Equity Fund

A collective investment scheme used to make investments in various equity (and, to a lesser extent, debt) securities according to one of the investment strategies associated with private equity.

Private Equity–Buyout

Equity investments, often coupled with debt financing, aimed at acquiring a majority interest in a company. The inclusion of debt can help investment fund managers enhance their equity returns by increasing internal rates of return on investor capital.

Private Equity Growth–Expansion

Later-stage investments in companies that, while already generating positive returns, are seeking to expand to the next stage or implement significant changes.

SBA Annual Financial Report (SBA Form 468)

The OII uses the Annual Financial Report to assess changes in SBICs while they participate in the program. SBICs submit them quarterly and they are audited annually.

SBA Portfolio Financing Report (SBA Form 1031)

The OII uses the Portfolio Financing Report to assess various characteristics of small businesses before their financing events. SBICs submit the form within 30 days of the close of financing. This form contains portfolio concern financing and supplementary information that the SBA uses to evaluate an SBIC’s investment activities and compliance with SBIC Program requirements. The agency also pools the information provided by individual SBICs on these forms to analyze the SBIC Program as a whole and the impact of SBIC financings on the growth of small businesses.

SBIC Funds (by Type)

Debenture: Debenture SBICs generally focus on later-stage, mezzanine, and buyout investments using primarily debt and hybrid financing

Non-leveraged: Non-leveraged SBIC funds make up approximately 15 percent of the active SBICs. Generally focused on later-stage, mezzanine, and buyout investments using primarily debt and hybrid financing, their private capital is not supplemented with SBAGuaranteed debentures.

Participating Securities: The SBIC Program’s participating securities effort was the SBA’s original attempt to infuse funding into the venture capital industry. It began in 1994, in time to catch the dot-com wave, and was suspended in 2004, when the SBA stopped issuing new licenses. Under the program, the SBA matched up to twice the amount of private capital raised by a qualified firm. Some venture capital businesses, such as Triathlon, which raised its debut fund under the initial program, succeeded, but others foundered.

Specialized: The specialized SBIC Program was authorized between 1969 and October 1996 to target “disadvantaged” businesses, meaning those that were at least 50 percent owned, controlled, and managed on a day-to-day basis by a person or persons whose

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participation in the free enterprise system was hampered because of social or economic disadvantages.

Small Business

A business with less than US\$19.5 million in tangible net worth AND an average after-tax income for the preceding two years of less than US\$6.5 million; OR, a business that qualifies as “small” under NAICS code standards (which are generally based on annual sales or the number of employees).

Venture Capital


Early-stage funding for startup companies that are high on risk but also high on potential. Venture capital is a type of equity financing that addresses 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 investments are generally made as cash in exchange for stock shares and an active role in the invested company.

Volcker Rule

A section of the Dodd-Frank Act, originally proposed by American economist and former Federal Reserve Chairman Paul Volcker to restrict U.S. banks from making certain kinds of speculative investments that do not benefit their customers.

Note: These definitions were compiled from various sources, including websites and official documents of U.S. government organizations, such as the Federal Financial Institutions Examination Council, the U.S. Census Bureau, the U.S. Small Business Administration, and the White House; the websites of trade associations, such as the National Association of Investment Companies and the National Venture Capital Association; and trade platforms, such as *Crunch Base* and *Investopedia*.

APPENDIX II. SBA PORTFOLIO FINANCING REPORT (SBA Form 1031)

	OMB No. 3245-0078 Expiration Date 10/31/2017																				
U.S. Small Business Administration Portfolio Financing Report																					
Name of Licensee _____ License Number _____																					
Part A - Small Business Concern Data																					
1. Name of Small Business _____ 2. Employer Identification Number ____ - ____ 3. Street Address _____ 4. City _____ 5. State _____ 6. ZIP Code _____ 7. County _____ 8. Small Business FAX _____ 9. Contact Person for FAX _____ 10. Date Business Established ____ / ____ / ____ 11. Form of Business ____ 1) Corporation 2) Partnership 3) Proprietor 4) LLC 12a. NAICS Code _____ Industry _____ 12b. Energy Saving Qualified Investment? ____ If checked, was Energy Saving debenture used to finance investment? ____ 13. Percentage of Small Concern (if any) Owned by: American Indian or Alaska Native: ____% Asian: ____% Black or African American: ____% Hispanic or Latino: ____% Native Hawaiian or Other Pacific Islander: ____% White: ____% 14a. Percentage of Small Concern Owned by Women (if any) ____% 14b. Percentage Owned by Veterans (if any) ____% 15. CEO or President (may select one or more): Woman: ____ American Indian or Alaska Native: ____ Asian: ____ Black or African American: ____ Hispanic or Latino: ____ Native Hawaiian or Other Pacific Islander: ____ White: ____																					
Part B - Prefinancing Information																					
16. Prefinancing Status: ____ (1) New Information (2) Previously Submitted (3) Acquired Business (4) New Business 17a. Stage of Company at Financing: _____ 17b. Technology developed with SBIR/STTR funding: _____ 18. Small Business Concern's Pre-Money Valuation: _____ 19. Fiscal Year End Immediately Prior to Date of Financing (Month/Day/Year) ____ / ____ / ____ 20. Gross Revenue for Prior Fiscal Year \$ _____ 21. After-Tax Profit or (Loss) for Prior Fiscal Year \$ _____ 22. Income Taxes for Prior Fiscal Year: Federal \$ _____ State \$ _____ Local \$ _____ 23. Net Worth \$ _____ 24. Number of Employees _____																					
Part C - Financing Information																					
25. a. Date of Financing ____ / ____ / ____ b. Date of Disbursement ____ / ____ / ____ 26. Did Licensee lead this investment? ____ 27. Purpose of Financing (Percentage of Financing that will be used to support each category below. Percentages should total to 100%.) <table style="width: 100%; border: none;"> <tr> <td style="width: 50%; vertical-align: top;"> a. Working Capital or Inventory Purchase _____ b. Plant Modernization or Leasehold Improvement _____ c. Acquisition of All or Part of an Existing Business _____ d. Consolidation of Obligations or Non-SBIC Debt Refunding _____ e. New Building or Plant Construction _____ </td> <td style="width: 50%; vertical-align: top;"> f. Acquisition of Machinery and Equipment _____ g. Land Acquisition or Dwelling Construction _____ h. Marketing Activities _____ i. Research and Development _____ j. Other _____ </td> </tr> </table>		a. Working Capital or Inventory Purchase _____ b. Plant Modernization or Leasehold Improvement _____ c. Acquisition of All or Part of an Existing Business _____ d. Consolidation of Obligations or Non-SBIC Debt Refunding _____ e. New Building or Plant Construction _____	f. Acquisition of Machinery and Equipment _____ g. Land Acquisition or Dwelling Construction _____ h. Marketing Activities _____ i. Research and Development _____ j. Other _____																		
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28. Is this the first Financing of this Small Business by the Licensee? ____																					
29. Financing Instruments and Applicable Amounts (for participations, include Licensee's portion only): <table style="width: 100%; border: none;"> <thead> <tr> <th style="text-align: left; border-bottom: 1px solid black;">Instrument</th> <th style="text-align: left; border-bottom: 1px solid black;">Amount</th> <th style="text-align: left; border-bottom: 1px solid black;">Initial Interest Rate(s)</th> <th style="text-align: left; border-bottom: 1px solid black;">% Actual Ownership</th> </tr> </thead> <tbody> <tr> <td>Loan Only</td> <td>\$ _____</td> <td>_____ %</td> <td></td> </tr> <tr> <td>Debt with Equity Features</td> <td>\$ _____</td> <td>_____ %</td> <td></td> </tr> <tr> <td>Equity Only</td> <td>\$ _____</td> <td></td> <td>_____ %</td> </tr> <tr> <td>Total Licensee Financing</td> <td>\$ _____</td> <td></td> <td></td> </tr> </tbody> </table>		Instrument	Amount	Initial Interest Rate(s)	% Actual Ownership	Loan Only	\$ _____	_____ %		Debt with Equity Features	\$ _____	_____ %		Equity Only	\$ _____		_____ %	Total Licensee Financing	\$ _____		
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Total Licensee Financing	\$ _____																				
30. Total Size of Financing Round for Small Business Concern: _____ 31. Comments: _____																					
Part D - Transmission Verification																					
Transmission Date ____ / ____ / ____																					

SBA Form 1031 (3/14) Previous Editions Obsolete

NOTE: REFER TO DISCLAIMER NOTICE

OMB No. 3245-0078 Expiration Date 10/31/2017
U.S. Small Business Administration Portfolio Financing Report
<p>Use of Information: SBA Form 1031 is to be completed only by small business investment companies (SBICs) licensed by the Small Business Administration (SBA). This form contains Portfolio Concern financing and supplementary information that SBA uses to evaluate an SBIC's investment activities and compliance with SBIC program requirements. SBA also pools information provided by individual SBICs to analyze the SBIC program as a whole and the impact of SBIC financings on the growth of small business.</p> <p>Instructions for Submitting Completed Form: SBA Form 1031 must be completed and filed electronically in the SBIC-Web system. SBIC-Web requires an SBA-approved user account. Submit your account request to sbicwebsupport@sba.gov.</p> <p>PLEASE NOTE: The estimated burden for completing this form is 12 minutes per response. You will not be required to respond to this information collection if a valid OMB approval number is not displayed. If you have questions or comments concerning this estimate or other aspects of this information collection, please contact the U.S. Small Business Administration, Chief, Administrative Information Branch, Washington, DC 20416 and/or SBA Desk Officer, Office of Management and Budget, New Executive Office Building, Room 10202, Washington, DC 20503.</p> <p style="text-align: center;">PLEASE DO NOT SEND FORMS TO OMB.</p>

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APPENDIX III. SBA ANNUAL FINANCIAL REPORT (SBA Form 468, Schedule 8)

SCHEDULE 8		Unaudited Portfolio Company Information				OMB Approval No. 3245-0063	
		AS OF				Expiration Date 10/31/2017	
Name of the Licensee:						License No.	

Portfolio Company Name	Employer ID	% Own	% Vote	Cost at End of Period	Unrealized App (Dep)	Total Reported Value
		0%	0%	\$0	\$0	\$0

General Portfolio Company Information Business Description: NAICS: <input style="width: 150px;" type="text"/> Soybean farming, field and seed production <hr/> 1st Date Invested: <input style="width: 80px;" type="text"/> Overline? <input style="width: 80px;" type="text"/> Current Stage: <input style="width: 150px;" type="text"/> Exchange: <input style="width: 80px;" type="text"/> Stock Symbol: <input style="width: 80px;" type="text"/> If original investment company's name changed, was acquired/merged, company name of original investment: <input style="width: 100px;" type="text"/> Address: <input style="width: 150px;" type="text"/> City/State: <input style="width: 100px;" type="text"/> Zip Code: <input style="width: 80px;" type="text"/> LMI: <input style="width: 80px;" type="text"/> Other Comments:	Portfolio Company Financial Information Rounded to nearest \$ Fiscal Year End: <input style="width: 100px;" type="text"/> <table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="width: 50%;"></th> <th style="width: 12.5%;">Period 1</th> <th style="width: 12.5%;">Period 2</th> <th style="width: 12.5%;">Period 3</th> </tr> </thead> <tbody> <tr> <td style="text-align: center;">As Of Date</td> <td></td> <td></td> <td></td> </tr> <tr> <td>Basis Period</td> <td></td> <td></td> <td></td> </tr> <tr> <td>Revenues</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>Gross Profit</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>EBITDA</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>Interest Charges</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>Net Income</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>Cashflow from Ops.</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>Burn Rate</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>Cash Balance</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>Current Assets</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>Fixed Assets</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>Total Assets</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>Current Liabilities</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>Debt</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>Total Liabilities</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>EOY Equity Value (Market)</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>EOY Enterprise Value</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td colspan="4">Full-time employees : -</td> </tr> <tr> <td colspan="2">Federal Taxes Paid : \$0</td> <td colspan="2">State Taxes Paid : \$0</td> </tr> </tbody> </table>		Period 1	Period 2	Period 3	As Of Date				Basis Period				Revenues	\$0	\$0	\$0	Gross Profit	\$0	\$0	\$0	EBITDA	\$0	\$0	\$0	Interest Charges	\$0	\$0	\$0	Net Income	\$0	\$0	\$0	Cashflow from Ops.	\$0	\$0	\$0	Burn Rate	\$0	\$0	\$0	Cash Balance	\$0	\$0	\$0	Current Assets	\$0	\$0	\$0	Fixed Assets	\$0	\$0	\$0	Total Assets	\$0	\$0	\$0	Current Liabilities	\$0	\$0	\$0	Debt	\$0	\$0	\$0	Total Liabilities	\$0	\$0	\$0	EOY Equity Value (Market)	\$0	\$0	\$0	EOY Enterprise Value	\$0	\$0	\$0	Full-time employees : -				Federal Taxes Paid : \$0		State Taxes Paid : \$0	
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In addition, the authors consulted relevant federal codes, laws, and regulations; U.S. government websites, such as those maintained by the Federal Deposit Insurance Corporation and the U.S. Small Business Administration; newspapers, such as the *Guardian*; and the websites of industry trade organizations, such as the National Association of Investment Companies and the National Venture Capital Association.

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