



The Small Business Investment Company (SBIC) Program

***Helping Meet the
Capital Needs of
America's Small
Businesses Since 1958.***

In FY 2013:

- *SBICs provided almost \$3.5 billion in financings*
- *SBICs financed 1,068 small businesses across the United States*
- *Operating at zero subsidy cost to the taxpayer*

Annual Report For Fiscal Year Ending September 30, 2013





Maria Contreras-Sweet
Administrator

U.S. Small Business
Administration

Message from the Administrator

The following report provides a comprehensive analysis of the Small Business Administration's (SBA) Small Business Investment Company (SBIC) program as part of our continued effort to deliver transparency, accountability and robust reporting on all of SBA's programs.

The report also highlights the success and progress the SBA has made in the past few years to streamline, simplify and strengthen its core programs. Today, the SBIC program serves as a model for public-private partnerships across the land.

Operating SBICs currently manage almost \$20 billion in private capital and SBA guaranteed leverage and commitments. In FY 2013, SBA licensed 34 SBICs with over \$1.2 billion in private investor capital, the highest private capital amount for a licensing cohort in the history of the program. More importantly, SBICs reported almost \$3.5 billion in financings to over a thousand small businesses, creating and sustaining jobs throughout the United States. That represents a 70% increase in financing dollars from three years ago and the highest amount of financings in over ten years.

It's important to note that the SBIC program is operated at zero subsidy cost to the taxpayer.

We will continue to build on the success of this program.

Sincerely,

A handwritten signature in blue ink that reads "Maria Contreras-Sweet".

Maria Contreras-Sweet
Administrator
U.S. Small Business Administration

**Javier Saade**

Associate Administrator for
Investment and Innovation

U.S. Small Business
Administration

Message from the Associate Administrator

The Office of Investment and Innovation of the U.S. Small Business Administration is proud to present the results of the Small Business Investment Company Program (SBIC) for Fiscal Year 2013. We continue to reach small businesses throughout the country, supporting U.S. jobs across diverse industries, including manufacturing, consumer and business services, transportation, technology, and health.

SBICs use privately raised capital plus SBA-guaranteed leverage to make investments in small businesses. Over the past 5 years, for every \$1 of SBA-guaranteed Debenture leveraged issued, SBICs provided over \$2 in financings.

Last year, the SBIC program provided almost \$3.5 billion in financings to 1,068 small businesses. Almost a quarter of these were businesses located in low or moderate income (LMI) areas or were women, minority, or veteran-owned businesses. One of our key goals is to reach farther into these and other underserved areas and under-represented groups.

The SBIC program grew in FY 2013, adding 34 new funds to its portfolio. These funds represented over \$1.2 billion in private capital, the highest private capital associated with newly licensed SBICs in a single fiscal year.

We recognize that, with growth, we need to be even more diligent with our licensing and monitoring processes. To enhance our monitoring processes, SBA launched a new web-based system in FY 2013 in order to improve financial data collection and analysis. SBA will continue to improve its web-based analytical tools in the coming years.

As a government program, SBA is committed to improving transparency and accountability. We hope the information in this report will help all stakeholders understand the SBIC program better.

Sincerely,

A handwritten signature in blue ink, appearing to be 'Javier Saade', written over a light blue grid background.

Javier Saade
Associate Administrator for Investment and Innovation
U.S. Small Business Administration

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SBIC Mission

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

(Section 102 of the Small Business Investment Act of 1958)

Goals

- Partner with privately owned and professionally managed funds.
- Increase access to private equity capital and long term loans for small businesses.
- Promote growth, expansion, and modernization in small businesses.
- Increase outreach to underserved markets.

1. Executive Summary

The Small Business Investment Company (SBIC) program guarantees leverage to licensed investment funds that in turn make loans and equity investments in small businesses. For over 55 years, SBICs have provided financing to thousands of small businesses, sustaining and creating jobs across the United States.

SBA accomplishes its mission by partnering with privately owned and professionally managed funds that provide financings, using privately raised capital and SBA-guaranteed leverage, to small businesses seeking growth capital, especially in markets where such capital is not adequately available. The program accomplishes these goals at zero subsidy cost to the taxpayer.

Over the past few years, SBA has focused on streamlining, simplifying and strengthening the SBIC program to better meet the needs of both investors and entrepreneurs. As part of this effort, SBA has been winding down the less effective Participating Securities program and expanding the Debenture SBIC program that has proven effective both economically and financially.

In FY 2013, the SBIC program grew to \$10.3 billion in Private Capital and \$9.5 billion in outstanding SBA leverage and commitments in 292 operating SBICs. Other program highlights for FY 2013 are noted below.

Exhibit 1-1 FY 2013 SBIC Program Highlights

Licensing	Operating / Execution	Impact
<ul style="list-style-type: none"> • Initial Review: SBA issued 31 Green Light¹ Letters to applicants • SBA licensed 34 SBICs, representing over \$1.2 billion in Private Capital <ul style="list-style-type: none"> - 15 First-time SBICs - 19 Subsequent SBICs (managers of prior or existing SBICs) 	<ul style="list-style-type: none"> • Approved \$2.2 billion in Debenture commitments to 68 SBICs • Examined 244 SBICs • Launched new web-based system to improve financial reporting and analysis. • Recovered SBA-guaranteed leverage and decreased the amount of outstanding leverage in the Office of SBIC Liquidations by 27% in the past three years. 	<ul style="list-style-type: none"> • SBICs provided almost \$3.5 billion in financings to 1,068 small businesses • Over 24% of businesses were women, minority, or veteran owned or in low or moderate income (LMI) areas • SBIC 2013 Financings created or sustained an estimated 73,585 jobs.

¹ SBICs are licensed via a 3-phase process: 1) Initial Review; 2) Capital Raise; and 3) Final Licensing. Applicants approved in Phase 1 by the Investment Committee are issued a “Green Light” letter which applicants use to raise private capital before applying for final licensing.



2013 SBIC of the Year
 Plexus Capital Partners
 Charlotte, NC

Plexus Capital Partners has 3 SBIC funds that have provided over \$300 million in financings to over 60 small businesses since 2006, creating and sustaining thousands of jobs. Plexus focuses on subordinated debt and equity investments in middle market companies. As a North Carolina based SBIC, Plexus makes many of its investments in the Southeast region of the United States.

Plexus Capital Managing Partner Bob Anders said, *“Being named the nation’s Small Business Investment Company of 2013 speaks to the value we are providing to our investors and small businesses across the country. We are very proud of this honor.”*

2. Introduction

In 1958, Congress created the SBIC program to “stimulate and supplement the flow of private equity capital and long-term loan funds” in order to bridge the financing gap between entrepreneurs’ need for capital and traditional financing sources. The SBIC program structure is unique in that, the SBA does not invest directly in small businesses, but provides SBA-guaranteed leverage to privately owned and professionally managed for-profit investment funds licensed by SBA. These licensed funds in turn make loans and investments into qualifying small businesses.

Exhibit 2-1: SBIC Public-Private Partnership Model



Private Investor’s Capital and SBA Guaranteed Leverage* is provided to the SBIC. The SBIC provides loans and investments to small businesses.

**SBICs may access leverage up to 3 times private capital (but typically 2 times), up to a maximum of \$150 million for a single SBIC and \$225 million for multiple SBICs under common control, subject to SBIC regulations and SBA credit policies*

This public-private partnership aligns the interests of all stakeholders to promote successful SBICs and financial and economic growth in the small businesses financed through the program. The SBIC program’s [website \(www.sba.gov/inv\)](http://www.sba.gov/inv) provides further information about the SBIC program.

This report discusses the SBIC operating portfolio, the economic impact of SBIC financings, SBA’s efforts to manage its SBIC portfolio, and the financial performance of the program and its portfolio. Although the report contains financial data, it has not been audited or peer reviewed. The intent is to increase program transparency and accountability to the public. Appendix A describes the methodology and sources for all charts and tables in this report.

2013 SBIC of the Year
*Blue Sage Capital
 Partners
 Austin, TX*

Blue Sage Capital has proven to be a leading participant in the SBIC program since Blue Sage's founding in 2003. Blue Sage's first fund invested over \$115 million in thirteen small businesses, working closely with management teams to professionalize and grow the business. Blue Sage has assisted the six companies that it has sold to date to increase revenues by 30% and increase EBITDA by 55%. Most important, these businesses grew the number of employees by 46% and created nearly 400 new jobs.

Co-Founder Peter Huff said, *"We are honored to have been chosen as SBIC of the Year. We pride ourselves on the impact we have made on the small business community through being 'good guys' that are easy to work with and by focusing on growing small companies."*

3. SBIC Operating Portfolio Overview

In FY 2013, SBA licensed 34 new SBICs with over \$1.2 billion in private capital, bringing the SBIC operating portfolio to 292 funds with \$10.3 billion in Private Capital and almost \$9.5 billion in SBA outstanding leverage and commitments for a total of \$19.8 billion of capital under management. These operating SBICs hold investments in thousands of companies in their portfolio, creating and sustaining thousands of jobs across the United States. The exhibit below provides a snapshot of the SBIC Program Operating Portfolio as of the end of FY 2013 by the type of SBA-guaranteed leverage security issued by the SBICs.

Exhibit 3-1: SBIC Program Operating Portfolio As of September 30, 2013 (Dollar Amounts in Billions)

	Operating SBICs	Debenture	Participating Securities	Other Funds
Number of SBICs	292	175	63	54
Private SBICs	\$10.33	\$7.50	\$1.32	\$1.51
SBA	\$9.48	\$8.40	\$1.02	\$0.06
Total	\$19.82	\$15.90	\$2.34	\$1.58

Notes: Capital includes both outstanding balances and unfunded commitments from Institutional Investors. "Other Funds" includes specialized SBICs (a type of SBIC that is no longer licensed) but may hold outstanding Debenture leverage and SBIC preferred stock (no longer issued) and "non-leveraged" SBICs that do not issue SBA leverage, but nonetheless play an important role in attracting private capital to small businesses in need of financing

As shown above, the majority of capital is held by SBICs that issue Debentures (Debenture SBICs).²

Debenture SBICs perform primarily mezzanine debt, senior loans, buyouts, and later stage or growth equity financings. The next chart provides a breakdown of outstanding SBA-guaranteed leverage for Operating Debenture SBICs by strategy as of September 30, 2013.

² As of October 1, 2004, the SBIC program underwent a major shift when SBA could no longer issue new commitments for Participating Securities leverage. The above numbers reflect SBA's efforts to increase capital to small businesses via its core Debenture program and responsibly wind-down the Participating Securities program.

Exhibit 3-2: Outstanding Leverage for Operating Debenture SBICs by Strategy (\$5.9 billion)
As of September 30, 2013³

Mezzanine	59.10%
Senior/Other Creditor	19.60%
Buyouts/Hybrid Strategy	21.30%
Total	100.00%

Despite periodic downturns in the capital markets over the past 20 years, the Debenture program remains strong. The following chart shows pooled one year rolling horizon internal rate of returns (IRRs) for SBICs issuing Debentures only (Debenture SBICs) licensed between calendar year 1998 and 2012 benchmarked against both Thomson's U.S. Private Equity and the S&P 500 Index.⁴

Exhibit 3-3: Pooled One Year Rolling Horizon IRRs for Debenture SBICs Licensed 1998-2012 (n=165)
As of December 31, 2012

	Year											
	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Debenture SBICs- Unleveraged	-2.2%	1.8%	6.1%	8.8%	15.8%	14.2%	8.1%	4.5%	3.5%	7.7%	9.8%	10.0%
Debenture SBICs-Private Investors	- 15.6%	-7.3%	5.2%	12.7%	31.3%	25.7%	10.6%	2.0%	0.3%	12.0%	16.0%	15.5%
Thomson U.S. All Private Equity	- 21.1%	- 12.4%	18.2%	20.3%	23.7%	21.5%	16.0%	22.9%	15.1%	18.2%	9.8%	13.5%
S&P 500 Index	- 11.9%	- 21.7%	29.0%	10.9%	4.9%	15.8%	5.2%	37.9%	27.2%	15.2%	2.3%	16.2%

The previous chart shows that the pooled Debenture SBIC performance on both an unleveraged and leveraged basis has generally followed industry trends since 2003. As a result of this performance and the structure of the Debenture security, the program continues to operate at zero subsidy cost to the taxpayer.

Given this robust performance, SBA has focused on growing its core Debenture program to continue to help entrepreneurs access needed growth capital. As shown in the next chart, SBA more than tripled the total capital under management⁵ of the Debenture program from \$4.7 billion in FY 2004 to \$15.9 billion by the end of FY 2013.

³ Leverage from Data Management's directory as of FY end 2013. Strategies are based on last year's benchmark data with new licensee strategies identified in consultation with Licensing.

⁴ SBIC unleveraged and private investor IRRs were calculated using the methodology described in Appendix A. Thomson and S&P 500 index data are from ThomsonOne.

⁵ Capital under management includes regulatory capital (generally, private capital and unfunded commitments from Institutional Investors) and SBA outstanding leverage and commitments.

Exhibit 3-4: SBIC Program Total Capital under Management (Private & SBA)
For Operating SBICs (In Billions of \$)⁶

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Debenture	\$4.9	\$4.9	\$5.4	\$6.1	\$6.9	\$7.6	\$9.1	\$11.1	\$13.3	\$15.9
Participating	\$15.5	\$13.9	\$12.5	\$11.2	\$8.8	\$7.4	\$5.7	\$4.5	\$3.5	\$2.4

Part of the reason for this growth may be due to the attractive economics of the SBA Debenture in recent years. The rate on SBA-guaranteed Trust Certificates, which determines the interest rates SBICs pay on SBA-guaranteed leverage, typically tracks the yield on the U.S. 10-year Treasury Note. As shown in the next chart, although these rates have been at historic lows in recent years, they rose slightly by the end of FY 2013.

Exhibit 3-5: SBA Debenture Coupon and Annual Charge Rates

Pricing Date	Date of Sale	Treasury Rate	Spread Above Treasury	Trust Certificate Coupon Rate
9/20/2001	9/26/2001	4.706%	1.180%	5.886%
3/18/2002	3/27/2002	5.313%	1.030%	6.343%
9/20/2002	9/25/2002	3.780%	0.890%	4.670%
3/19/2003	3/26/2003	3.938%	0.690%	4.628%
9/16/2003	9/24/2003	4.285%	0.590%	4.875%
3/17/2004	3/24/2004	3.675%	0.463%	4.120%
9/15/2004	9/22/2004	4.166%	0.518%	4.684%
3/15/2005	3/23/2005	4.540%	0.498%	5.038%
9/20/2005	9/28/2005	4.267%	0.674%	4.941%
3/15/2006	3/22/2006	4.729%	0.795%	5.524%
9/20/2006	9/27/2006	4.717%	0.818%	5.535%
3/20/2007	3/28/2007	4.543%	0.833%	5.376%
9/18/2007	9/26/2007	4.493%	1.035%	5.528%
3/18/2008	3/26/2008	3.393%	2.078%	5.471%
9/18/2008	9/24/2008	3.452%	2.273%	5.725%
3/18/2009	3/25/2009	2.942%	1.678%	4.620%
9/16/2009	9/23/2009	3.468%	0.765%	4.233%
3/17/2010	3/24/2010	3.642%	0.466%	4.108%
9/15/2010	9/22/2010	2.670%	0.545%	3.215%
3/22/2011	3/29/2011	3.341%	0.743%	4.084%
9/12/2011	9/21/2011	1.954%	0.923%	2.877%
3/14/2012	3/21/2012	2.263%	0.503%	2.766%
9/11/2012	9/19/2012	1.695%	0.550%	2.245%
3/20/2013	3/27/2013	1.939%	0.412%	2.351%
9/17/2013	9/25/2013	2.859%	0.785%	3.644%

⁶ From Data Management FY End directory tables. Debenture funds are identified as all SBICs with the fund type "Debenture" and all Bank-owned SBICs that have either outstanding Debentures or Debenture commitments. Participating funds are identified as all SBICs with the fund type "Participating" indicating the SBICs is licensed to issue Participating Securities.

Federal FY Commitment Obligated	Date of Leverage Commitment	Annual Charge - Participating Securities	Annual Charge - Debentures
FY 1999	10/1/98 - 9/30/99	1.000%	1.000%
FY 2000	10/1/99 - 9/30/00	1.000%	1.000%
FY 2001	10/1/00 - 9/30/01	1.000%	0.880%
FY 2002	10/1/01 - 9/30/02	1.376%	0.866%
FY 2003	10/1/02 - 9/30/03	1.311%	0.887%
FY 2004	10/1/03 - 9/30/04	1.454%	0.855%
FY 2005	10/1/04 - 9/30/05	N/A	0.871%
FY 2006	10/1/05 - 9/30/06	N/A	0.941%
FY 2007	10/1/06 - 9/30/07	N/A	0.906%
FY 2008	10/1/07 - 9/30/08	N/A	0.717%
FY 2009	10/1/08 - 9/30/09	N/A	0.406%
FY 2010	10/1/09 - 9/30/10	N/A	0.285%
FY 2011	10/1/10 - 9/30/11	N/A	0.515%
FY 2012	10/1/11 - 9/30/12	N/A	0.804%
FY 2013	10/1/12 - 9/30/13	N/A	0.760%

Note: The annual charge on a debenture or participating security depends on the Federal fiscal year the leverage commitment was obligated by SBA, regardless of the date that the leverage was drawn by the SBIC

Most importantly, due to increased capital in the program, the amount of SBIC financings to small businesses has grown significantly, with total SBIC financing dollars in FY 2013 outpacing any other fiscal year in over 10 years, despite the continuing wind-down of the Participating Securities program.

**Exhibit 3-6: Amount of SBIC Financings Reported by Fund Type and Fiscal Year
(In Millions of \$)**

	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Debenture	\$1.20	\$1.28	\$1.44	\$1.23	\$1.58	\$2.59	\$2.95	\$3.26
Participating	\$1.48	\$1.24	\$0.84	\$0.46	\$0.34	\$0.16	\$0.10	\$0.08
All SBICs	\$2.89	\$2.64	\$2.43	\$1.86	\$2.05	\$2.83	\$3.23	\$3.50

The next section provides further information on SBIC financings and the program's economic impact.



SMS Assist, LLC

Chicago, Illinois

SMS Assist founder Michael Rothman developed a proprietary technology platform that transformed a brick and mortar facilities maintenance company into a distributed outsourcing model with over 28,000 certified affiliates made up of entrepreneurs. SMS leverages its infrastructure to provide multi-location, national customers with consolidated management of the facilities maintenance function, including integrated billing, compliance reports, service tracking, and quality control.

SMS's capital base was strained by developing the software platform, hiring industry experts, and growing the customer base. That's when SBIC fund Granite Creek FlexCap I, L.P. invested interest-only mezzanine debt in the company. GraniteCreek was the first institutional investor in SMS and helped the company build a Board of Advisors, recruit new senior management, and obtain additional debt and equity capital.

SMS services 50,000 location sites across the U.S. and performed over 500,000 unique services in 2013. Since Granite Creek's investment, SMS revenue has tripled and the number of employees has exploded from 36 to 250.

4. SBIC Financings and Economic Impact

a. SBIC Financing Trends

As shown in the chart below, the amount of SBIC financings provided has grown rapidly since FY 2009.

Exhibit 4-1: Amount of SBIC Financings by Fiscal Year (\$ Millions)

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Total SBIC Financings	\$1,856.10	\$2,047.10	\$2,833.40	\$3,227.40	\$3,498.30
BDC-SBIC Financings	\$406.90	\$617.90	\$1,142.60	\$919.90	\$1,051.10

Part of the reason for this increase is due to SBICs whose private capital is funded by publicly owned Business Development Companies (BDCs). Because these BDCs are public, they are able to access capital quickly. Consequently, "BDC-SBICs" average \$46.6 million in private capital per SBIC while other SBICs averaged \$34.5 million per SBIC as of the end of FY 2013.

As a result of increased interest by BDCs, since FY 2009 BDC-SBIC financings grew 158% versus 88% for the overall program. By the end of FY 2013, 22 BDC-SBICs held over 25% of SBA's outstanding Debenture leverage and provided over 30% of SBIC financing dollars.

Although SBIC financing amounts have risen, the number of small businesses financed by SBICs has slightly decreased, as shown in the next chart.

Exhibit 4-2: Number of Small Businesses Financed by SBICs by Fiscal Year Reported

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
All SBICs/SBIC Types	1,481	1,330	1,339	1,094	1,068
SBIC Types Currently Licensed	1,042	976	1,096	896	942

**"SBIC Types Currently Licensed" only includes SBICs issuing Debentures only (Debenture SBICs) and non-leveraged SBICs. This excludes SBICs that issued Participating Securities and Specialized SBICs, which SBA no longer licenses. The intent is to separate core SBIC program performance from programs winding down or no longer being licensed.*

Although most of this decrease is due to the wind-down of the Participating Securities program, the number of businesses funded by Debenture and non-leveraged SBICs has also decreased since 2009. Since the number of business has decreased and the financing dollars have increased, the average financing size has more than doubled from \$1.3 million in FY 2009 to \$3.3 million in FY 2013.

Exhibit 4-3: Average SBIC Financing Amount to a Small Business by Fiscal Year Reported (\$ Millions)

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Average SBIC Financing Amount	\$1.3	\$1.5	\$2.1	\$3.0	\$3.3

This increase in financing size may be due in part to the types of financing provided by SBICs in recent years. SBICs provide loans (senior and sub-debt), as well as mezzanine debt with equity features such as warrants or convertible debt, and equity. As shown in the chart below, both SBIC equity financings and mezzanine debt have remained relatively stable since FY 2009, while SBIC financings in the form of loans has grown by 271% since FY 2009.

Exhibit 4-4: SBIC Financings by Financing Type and Fiscal Year Reported (\$ Millions)

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Loans	\$564.40	\$803.80	\$1,375.20	\$1,927.70	\$2,095.70
Debt w/equity	\$718.20	\$772.30	\$1,022.90	\$723.30	\$834.10
Equity	\$573.50	\$471.00	\$435.20	\$576.40	\$568.50
TOTAL Financings	\$1,856.10	\$2,047.10	\$2,833.40	\$3,227.40	\$3,498.30

This increase in SBIC loan financings may be due to the lack of available loans from traditional sources during these years. The Pepperdine Private Capital Markets Project 2013 Capital Markets Report indicated that based on a survey of 190 Investment Bankers, *“Respondents indicated a general difficulty with arranging senior debt for businesses with less than \$5 million in EBITDA [Earnings before Interest, Tax, Depreciation and Amortization].”*⁷ The National Small Business Association June 2013 Mid-Year Economic Report indicated, *“Today, just 65 percent of small businesses report they are able to obtain adequate financing, down from 73 percent six months ago.”*⁸ SBICs targeted this gap in the capital markets.

For the five year period FY 2009-2013, SBICs provided financings across the United States to diverse industries as shown in the charts on the next page.

⁷ Paglia, John (2013), Pepperdine University Graziadio School of Business and Management, **“Pepperdine Private Capital Markets Project, 2013 Capital Markets Report”**, page 12, Retrieved from <http://bschool.pepperdine.edu/appliedresearch/research/pcmsurvey/content/2013PPCMPcapital-markets-report.pdf>

⁸ National Small Business Association (June 2013), **“2013 Mid-Year Economic Report”**, page 10, Retrieved from <http://www.nsba.biz/wp-content/uploads/2013/08/2013-MY-Report1.pdf>

Exhibit 4-5: Distribution of SBIC Financing Dollars by Geography Reported FY 2009-2013
 Total SBIC Financings = \$13.5 Billion

Location	Percentage
Pacific	15.60%
Mountain	7.50%
West North Central	5.20%
West South Central	11.00%
East South Central	3.60%
East North Cenral	11.40%
New England	8.90%
Middle Atlantic	19.00%
South Atlantic	17.80%
TOTAL	100.00%

Exhibit 4-6: Distribution of SBIC Financing Dollars by Industry Reported FY 2009-2013
 Total SBIC Financings = \$13.5 Billion

Location	Percentage
Manufacturing	26.00%
Professional, Scientific, and Technical Services	14.00%
Information	12.00%
Transportation and Warehousing	8.00%
Health Care and Social Assistance	7.00%
Wholesale Trade	7.00%
Other	26.00%
TOTAL	100.00%

b. SBIC Financings Meeting the Needs of Underserved Markets

The SBIC program’s mission is to "supplement the flow of private equity capital and long-term loan funds” to small businesses “which are not available in adequate supply”.

Businesses in “competitive opportunity gaps”, defined as [low and moderate income areas](#) and businesses majority owned by women, minorities, and veterans, have traditionally had problems accessing capital. As shown in the chart below, both the number and percentage of SBIC financings to these groups have slightly decreased in recent years. This is partially due to fewer operating Specialized SBICs, which targeted disadvantaged groups but which SBA no longer has authority to license. By the end of FY 2013, there were only 11 Specialized SBICs with less than \$200 million in private capital and SBA leverage and commitments.

Exhibit 4-7: Small Businesses in “Competitive Opportunity Gaps” Financed by SBICs by Fiscal Year

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Low & Moderate Income (LMI)	321	318	351	216	213
Women, Monority, or Veteran Owned	164	109	110	108	67
% in Competitive Opportunity Gaps	29.80%	29.50%	32.10%	26.50%	24.30%

*“Competitive Opportunity Gaps” is defined as small businesses in low and moderate income areas or majority owned by women, minorities, or veterans.

In FY 2014, SBA will review its policies to explore ways in which to encourage SBICs to increase financings in these areas.

However, “Competitive Opportunity Gap” businesses are not the only businesses suffering from problems in accessing capital. The [Pepperdine Private Capital Markets Project 2013 Capital Markets Report](#) indicated a “general imbalance between companies worthy of financing and capital available for the same. There is a reported shortage of capital for those with less than \$10 million in EBITDA [but a general surplus for companies with \$10 million in EBITDA or more.”⁹ Since SBICs make investments in small businesses, SBICs naturally fill this gap.

Although SBA does not currently capture EBITDA at the time of SBIC financing¹⁰, the following chart shows the distribution of FY 2013 SBIC financing dollars by portfolio company net income. With over 90% of SBIC financing dollars going towards businesses with less than \$5 million in net income, the majority of SBIC investment dollars are directed towards the financing gap identified by Pepperdine’s report.

Exhibit 4-8: Distribution of Reported FY 2013 SBIC Financing Dollars by Portfolio Company Net Income *

Net Income	Percentage
Net Income Greater than \$10 Million	2.02%
Net Income Between \$5 and 10 Million	5.12%
Net Income Between \$1 and 5 Million	37.73%

* Portfolio company net income is derived from SBIC data provided in SBA Form 1031, SBIC Financing Data. The distribution only includes those portfolio companies in which SBICs reported net income data. SBICs are not required to provide this information if this is a follow-on financing and data was previously submitted. Many SBICs performing follow-on financings continued to provide this information. Approximately 12% of the financing dollars were associated with financings that did not report net income.

⁹ Paglia, John (2013), Pepperdine University Graziadio School of Business and Management, “Pepperdine Private Capital Markets Project, 2013 Capital Markets Report”, page 12, Retrieved from <http://bschool.pepperdine.edu/appliedresearch/research/pcmsurvey/content/2013PPCMPcapital-markets-report.pdf>.

¹⁰ SBA’s new web-based system will capture EBITDA as part of the FY 2013 Annual Form 468 SBIC Financial Reporting.

SBICs also provide financing to geographic areas of the country that typically do not obtain private equity capital investment. As shown below, Private Equity financings are geographically concentrated in 15 counties, which receive over half of all private equity financing dollars. SBICs provide 75% of SBIC financing dollars to other counties and over 62% of SBIC dollars went to counties that received less than half that proportion of Private Equity financings overall.

Exhibit 4-9: Geographic Comparison of SBIC Financings to Private Equity Industry* (FY 2009-2013)

	Private Equity Industry	SBIC Financings
All Other Counties	31.23%	62.96%
Next 15 Counties	17.35%	12.10%
Top 15 Counties	51.42%	25.00%

* Based on Thomson One U.S. private equity financing data.

c. Jobs

According to the [Pepperdine Private Capital Markets Project 2013 Capital Markets Report](#), surveyed business owners indicated that the number one policy that would most likely lead to job creation was “increased access to capital”.¹¹ The [2012 Small Business Access to Capital Survey](#) performed by the National Small Business Association identified that 53% of small businesses in which access to capital was a problem stated that as a result they were unable to grow or expand operations and 32% reduced the number of their employees.¹² The SBIC program addresses the need for growth capital and proves how capital translates to jobs. The chart below indicates that based on SBA estimates, SBIC financings in FY 2013 created or sustained over 73,000 jobs, a 20% increase over the last two years.

Exhibit 4-10: SBIC Estimated Jobs Created or Sustained

	FY 2011	FY 2012	FY 2013
Estimated Jobs Created Or Sustained	61527	68918	73585

* SBA estimates jobs created or sustained using the results of two studies on the impact of venture capital on employment. These studies estimate that one job is created or sustained for every \$36,000 invested (adjusted for inflation). Studies: 1) DRI-WEFA, “Measuring the Importance of Venture Capital and Its Benefits to the United States Economy,” June 19, 2002. 2) Cook & Nevins. The Zermatt Group. “The 1999 Arizona Venture Capital Impact Study,” March 1999)

As noted in the chart, SBA estimates jobs using, in part, a 1999 study on venture capital. SBA is currently seeking to replace this method for estimating jobs as this study is dated and may not be directly applicable to SBICs. Although SBA collects job numbers from its SBICs for its portfolio companies, SBA is considering changes to provide higher confidence in job numbers.

¹¹ Paglia, John (2013), Pepperdine University Graziadio School of Business and Management, “Pepperdine Private Capital Markets Project, 2013 Capital Markets Report”, page 74, Retrieved from <http://bschool.pepperdine.edu/appliedresearch/research/pcmsurvey/content/2013PPCMPcapital-markets-report.pdf>.

¹² National Small Business Association (2012), Small Business Access to Capital Survey, page 4, Retrieved from <http://www.nsba.biz/wp-content/uploads/2012/07/Access-to-Capital-Survey.pdf>.

Air Serv Corporation

Atlanta, Georgia

Air Serv was founded in 2002 to provide commercial airlines, airports, and transportation companies in the U.S. with services ranging from detailing the interior of aircraft to assisting guests with special needs. The company actively deployed mobile technology through its workforce to be a cost-effective provider of outsourced services, and grew rapidly from 2002 to 2010. In 2010 Air Serv sought to implement its operating model in ancillary janitorial businesses.

SBIC fund Petra Capital stepped in to provide preferred stock and subordinated debt capital to fund Air Serv’s growth objectives, including an acquisition that expanded the business to non-airline janitorial services. Petra Capital actively served on the Board of Directors and assisted the company in expanding its senior debt facility and identifying other acquisition opportunities.

From 2010 to 2012, Air Serv’s revenue grew at a 23% CAGR and EBITDA margins expanded with scale. In 2012 Petra Capital assisted with the sale of the company to ABM Industries Inc., a publicly traded company on the NYSE; Air Serv was combined with ABM’s existing airline services division creating a \$650 million revenue business unit under the leadership of Air Serv management.

5. SBIC Program Execution

The SBA’s Office of Investment and Innovation (OII) administers the SBIC program throughout the SBIC lifecycle as shown in the chart below.

Exhibit 5-1: SBA Key Activities in SBIC Lifecycle

1. Licensing	2. Operating	3. Fund Resolution
<ul style="list-style-type: none"> Initial Review SBIC Regulations Class Final Licensing 	<ul style="list-style-type: none"> Funding (leverage) Monitoring Regulatory Approvals Examinations 	<ul style="list-style-type: none"> Leverage Repayment and SBIC Surrender Liquidation Activities (in case of defaults)

This section discusses key SBA activities in FY 2013 to grow and oversee the program.

a. Licensing Activities

The chart below shows the phases and timeframes in the SBIC licensing process.

Exhibit 5-2: SBIC Licensing Process

SBA Decision Point: “Green Light” Letter	SBA Decision Point: Licensing Decision	
Phase I: Initial Fund Review	Phase II: Private Capital Raise	Phase III: Final Licensing
<i>Goal: 45 working days (approximately 2 months)</i>	<i>Up to 18 months</i>	<i>Goal: 6 months</i>

SBIC program growth is due to increased interest in the SBIC program by qualified fund managers. As shown in the following chart, in FY 2010, the number of SBIC applications received by SBA increased by over 50% and has remained relatively stable since then. This increase in applications, however, did not translate to an increase in the number of green lights issued, although more of the applicants that received a green light raised sufficient private capital to submit applications for Phase III Final Licensing.

Exhibit 5-3: SBIC Licensing Pipeline Volume by Fiscal Year

	2009	2010	2011	2012	2013
Application Received in Phase I - Initial Fund Review	48	73	74	61	71
Green Light Letters issued	36	40	40	38	31
Applications Received in Phase III - Final Licensing	Not Available	15	33	36	47
New SBIC Licensees	11	23	22	30	34

As shown above, the number of new SBIC licensees tripled between 2009 and 2013. Although 72% of the initial applications received in Phase I during this timeframe were from first-time SBIC applicants, only 45% of the new licensees were first-time SBICs. As shown below, funds seeking a subsequent SBIC license have a higher approval rate (percent of Phase I applications processed that received green light letters).

Exhibit 5-4: Phase I Approval Rate for Initial Applications Processed Between FY 2009 and 2013
(Approval Rate = Percent of Initial Applications Processed by SBA in Phase I That Received Green Light Letters)

	Percent
1st Time SBIC Applicants (n=228)	51.80%
Subsequent Fund Applicants (n=91)	73.60%
Overall (n=319)	58.00%

Approximately 80% of the final applications processed in Phase III – Final Licensing between FYs 2009 and 2013 received an SBIC license. The quality of SBA’s licensing process can be measured by the SBIC program’s financial health and how its portfolio tracks to relevant industry metrics, discussed in [Section 6](#).

In order to maintain high licensing standards, SBA processing times slightly increased between FY 2012 and 2013 due to increased volume in applications. Although SBA will continue to seek ways to streamline its processes, SBA cannot sacrifice standards of quality in its analysis and due diligence.

Exhibit 5-5: SBIC Licensing Process Times by FY

Phase I Initial Review Average Months to Process				
FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
2.7	3.5	3.5	2.2	2.8
	1.2	0.6	1.1	0.7

Initial 2 month goal FY2009 and subsequent 1 month goal starting FY2010.

Phase III Final Licensing Average Months to Process

FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
14.6	5.8	5.6	5.8	6.8

Six month goal

* SBA sets two processing time goals for Phase I – Initial Review. Because SBA is familiar with the performance of current or prior SBIC managers seeking a subsequent SBIC license, SBA’s processing time goal is 1 month. For 1st time SBIC applicants, SBA’s goal is 2 months since more due diligence and analysis is required. No such distinction is made in Phase III Final Licensing since a significant portion of the time is spent reviewing legal documents.

Most importantly, the amount of private capital associated with new SBICs more than tripled between FYs 2009 and 2013, making it the highest in any licensing year in the history of the program. The chart below shows the initial private capital for SBICs licensed in the past 15 years.

Exhibit 5-6: Initial Private Capital for New SBIC Licensees by FY Licensed (In \$ Million)

	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Participating	\$451	\$819	\$921	\$600	\$507	\$904	No further Participating Securities SBICs Authorized								
Non leveraged/Bank-owned	\$216	\$148	\$45	\$39	\$7	\$61	\$52	\$5	\$161	\$8	\$88	\$39	\$127	\$81	\$147
Debenture	\$81	\$230	\$136	\$160	\$230	\$83	\$269	\$341	\$218	\$232	\$257	\$616	\$714	\$893	\$1,112
Total Initial Private Capital	\$747	\$1,197	\$1,102	\$799	\$743	\$1,047	\$320	\$346	\$378	\$240	\$345	\$655	\$840	\$974	\$1,259

Note: No further Participating Securities SBICs Authorized beyond 2004

b. Operating

Once a fund receives its SBIC license, SBA assigns an analyst from OII’s Office of SBA Operations (Operations) who serves as the primary point of contact for the SBIC, answering any questions, monitoring fund performance, handling leverage requests, and processing any approvals required by regulation.

SBA processed over \$2.1 billion in aggregate SBA leverage commitments in FY 2013 to 68 SBICs, up 12% from the prior year and more than double the amount of commitments five years ago. SBA’s improved commitment processing times contributed to this growth. As shown below, SBA’s time to process a commitment has dropped by more than half since FY 2010, with SBA processing all FY 2013 commitment applications within its 2 month goal.

Exhibit 5-7: SBA Leverage Commitment Metrics

SBA Debenture Commitments Approved

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
SBICs	33	44	45	57	68
Commitments Approved	\$788.00	\$1,164.80	\$1,827.50	\$1,924.10	\$2,155.70

Average Months to Process Commitment (Goal: 2 months)

	FY 2010	FY 2011	FY 2012	FY 2013
SBICs	44	45	57	68
Months	2.2	1.3	1	1

This increase in commitments has led to the highest SBA outstanding leverage and commitments in SBA's operating portfolio in over five years. By the end of FY 2013, Operations monitored 292 SBICs with over \$9.6 billion in outstanding SBA guaranteed leverage and commitments.

Exhibit 5-8: SBIC Operating Portfolio Outstanding SBA Leverage & Commitments by FY (\$ Millions)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Specialized	\$0.07	\$0.07	\$0.03	\$0.03	\$0.02	\$0.02	\$0.01	\$0.02	\$0.02	\$0.02
Participating	\$9.81	\$8.67	\$7.60	\$6.69	\$4.84	\$4.03	\$3.01	\$2.24	\$1.57	\$1.05
Debentures	\$2.57	\$2.48	\$2.74	\$3.10	\$3.67	\$4.15	\$4.89	\$6.00	\$7.23	\$8.40
TOTAL	\$12.45	\$11.22	\$10.38	\$9.81	\$8.53	\$8.20	\$7.91	\$8.25	\$8.82	\$9.52

Given the number of new licensees in recent years and the licensing pipeline, SBA expects this upward trend to continue in FY 2014. With this amount of capital at risk, SBA closely monitors the portfolio's financial health (see [Section 6](#)).

To help SBA monitor the financial health of its SBIC portfolio, in FY 2013 OII's Data Management Division launched a web-based system to collect and analyze important financial information. OII also updated its external website (www.sba.gov/inv) to provide SBICs access to all statutes, regulations, policies, and forms associated with the program and to provide answers to frequently asked questions.

Another important monitoring tool SBA uses is examinations performed by OII's Office of SBIC Examinations. In FY 2013 SBA examined 206 leveraged licensees (SBICs with outstanding leverage, commitments, or earmarked assets) and 38 licensees without leverage. Although the Small Business Investment Act of 1958, as amended requires SBA to examine licensees at least every two years, SBA's goal is to examine leveraged SBICs on a 12-month cycle and those without leverage on an 18-month cycle. As shown in the next chart, SBA has maintained this goal for the past 3 years.

Exhibit 5-9- SBIC Examination Cycle by FY (in Months)

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Leverage (months)	13.9	12.9	11.7	11.7	11.6
Without Leverage (Months)	21.20	18.20	15.60	15.60	16.50

In order to help SBICs avoid problems in exams, SBA publishes a list of common exam findings at <http://www.sba.gov/content/sbic-examination-faqs#commonfindings>.

c. Fund Resolution

Most SBIC funds are structured as limited partnerships that surrender their license after the SBIC repays its SBA-guaranteed leverage,¹³ typically 10-15 years after licensed. In FY 2013, 27 SBICs surrendered their SBIC license, up 59% from FY 2012 primarily due to the wind-down of the Participating Securities Program.

¹³ SBICs that issued Participating Securities also must liquidate all "earmarked assets".

If SBICs have regulatory problems that cannot be resolved in Operations, SBA has the authority to transfer the SBIC to the Office of SBIC Liquidations (Liquidations) where Liquidations staff proceed to recover SBA leverage and minimize losses.

In FY 2013 Operations transferred 16 SBICs, representing \$415.6 million in SBA leverage, a 14% increase from the prior year. Three quarters of the transferred SBICs were Participating Securities SBICs. Despite this increase in transfers, Liquidations collected and charged off over \$470 million in leverage in FY 2013, to bring the overall balance of leverage in Liquidations down by 3% from last FY and down 27% from FY 2010. This trend is shown in the next chart.

Exhibit 5-10- Outstanding Leverage in Office of SBIC Liquidations by FY End

	2009	2010	2011	2012	2013
Debentures & Preferred Stock	\$221.36	\$300.10	\$222.80	\$310.80	\$343.80
Participating	\$1,429.00	\$1,585.00	\$1,406.50	\$1,111.70	\$1,008.20
TOTAL	\$1,650.60	\$1,885.10	\$1,629.30	\$1,422.50	\$1,352.00

Between FYs 2009 and 2013, Liquidation staff recovered over \$1.1 billion in leverage. These recoveries are critical to keeping the program at zero cost to the taxpayer.

The next section discusses the financial health of the SBIC program and its portfolio.

**SBIC Financial Risk and Performance
FY 2013 Highlights**

- *Debenture SBIC program continues to operate at zero subsidy cost to the taxpayer.*
- *Percentage of Debenture leverage out of regulatory compliance (in Liquidations or capially impaired) rose to 7% in FY 2013, still within historical averages.*
- *Underlying Debenture SBIC pooled performance commensurate with industry private equity benchmarks (Preqin and Thomson One)*
- *Debenture SBIC 10 year horizon pooled returns for SBICs Licensed 1998-2012 (as of 12/31/2012)*
 - *Unleveraged: 8.7%*
 - *Private Investor: 12.9%*
- *Percentage of Debenture SBICs in top half of industry based on unleveraged performance has steadily increased since 1998.*

6. SBIC Financial Risk and Performance

a. SBA’s Financial Risk and Performance

SBA’s Office of the Chief Financial Officer (OCFO) performs estimates for the SBIC program each fiscal year and analyzes the SBIC program’s loan performance each year to determine whether the program is performing within original estimates and to formulate models that determine the annual fee for the program. As of FY 2013, the Debenture program continues to perform within estimates on a lifetime basis, while the Participating Securities program is expected to produce significant losses.¹⁴ This performance disparity is reflected by SBA’s capital at risk as of September 30, 2013.

**Exhibit 6-1- SBA Capital at Risk by Leverage Type
As of September 30, 2013 (In Millions of \$)**

	Debentures	Participating Securities
Unreimbursed Prioritized Payments	\$ -	\$238.30
Unfunded SBA Leverage Commitments	\$2,545.20	\$ -
Leverage Operations	\$6,174.50	\$912.20
Leverage in Liquidations	\$343.80	\$1,008.20
Total Capital at Risk	\$9,063.40	\$2,158.70

The primary reason SBICs are transferred to the Office of Liquidations is due to significant losses in the SBIC’s portfolio that result in an SBIC being capially impaired. As shown, of the over \$9 billion in leverage and commitments outstanding, only 5.3% is managed by Liquidations. With over half of the leverage in the Participating Securities program in Liquidations, SBA continues to wind down that program.

Since the Participating Securities program is rapidly winding down and current authorizations for SBIC leverage only permit Debenture leverage, the remainder of the analysis in this section will focus primarily on Debenture SBICs.

¹⁴ SBIC program re-estimates and formulation information may be found in the Federal Credit Supplement worksheets to the Federal Budget at <http://www.whitehouse.gov/omb/budget/Supplemental>.

SBA analysts use a variety of metrics to evaluate the performance of operating SBICs, including valuations, recoverable SBIC assets to leverage, Debenture interest coverage, and capital impairment percentage (CIP).¹⁵ However, CIP is the primary regulatory metric by which SBA may transfer an SBIC to Liquidations. The chart below shows the status of outstanding Debentures and Preferred Stock for Operating Debenture and Specialized SBICs¹⁶ for the past several years for Debenture and Specialized SBICs.

Exhibit 6-2- Status of Outstanding Debentures & Preferred Stock for Debenture and Specialized SBICs

	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Under Max CIP	\$2,510.0	\$2,893.0	\$3,411.0	\$4,249.0	\$4,852.8	\$5,966.5
Over Max CIP	\$92.0	\$31.0	\$23.0	\$22.0	\$32.6	\$114.4
In Liquidations	\$156.0	\$219.0	\$290.0	\$213.0	\$298.0	\$343.8
Total Leverage	\$2,758.0	\$3,143.0	\$3,724.0	\$4,484.0	\$5,184.4	\$6,424.7
% out of Compliance	9.00%	8.00%	8.00%	5.00%	6.00%	7.00%

**“Out of Compliance” includes leverage associated with SBICs in Liquidations and SBICs in Operations over their maximum CIP (capitally impaired).*

As shown above, although in recent years the amount of leverage associated with SBICs out of compliance (capitally impaired SBICs and SBICs in Liquidations) has increased, the percentage of leverage out of compliance remains within historic averages. Because it typically takes several years before a Debenture fund may become capitally impaired, the median age of transfer to Liquidations for Debenture SBICs is 9 to 10 years.¹⁷ As a result, the SBIC program’s significant growth in the past five years may be contributing to this low percentage since younger funds are typically too early to become capitally impaired. As of the end of September 30, 2013, over two-thirds of Debenture outstanding leverage was held by funds licensed in the past five years.

The next chart shows the status of all leverage issued by SBICs licensed since 1994. This chart shows both the growth in the program in recent years and the natural progression of repayment and impairment by age.

¹⁵ Capital Impairment Percentage (CIP) measures the losses incurred by a fund relative to its Regulatory Capital, as defined under 13 CFR 107.50. SBIC regulations establish a maximum allowable CIP. If an SBIC exceeds its maximum, SBA has the right to transfer the SBIC to Liquidations.

¹⁶ As of September 30, 2013, Specialized SBICs had less than \$30 million in outstanding Debenture leverage and preferred stock.

¹⁷ Based on the age of all Debenture SBICs transferred to Liquidations and licensed after 1980.

Exhibit 6-3- Status of all Debenture Leverage Issued by Debenture SBICs Licensed since FY 1994 by Age or FY Licensed As of 9/30/2013 (In \$ Millions)

	Less Than 5 Years (2009-2013)	5 to 10 years old (2004-2008)	10 to 15 years old (1999-2003)	15 to 20 years old (1994-1998)
Repaid	\$35.0	\$996.4	\$1,449.5	\$408.9
Not Impaired Outstanding	\$3,963.9	\$1,424.3	\$358.1	\$ -
Impaired Outstanding	\$ -	\$113.2	\$ -	\$ -
Transferred to Liquidations	\$ -	\$88.7	\$76.4	\$338.5
Total Issued	\$3,998.9	\$2,622.6	\$1,883.9	\$747.4
% Transferred or Impaired	0.0%	7.7%	4.1%	45.3%

One can see from the above chart that SBICs under 5 years old are still in their Investment stage and continue to draw leverage to make investments. They typically begin to harvest their investments after 5 years and wind down after 10 years. After 15 years, most SBICs either repaid their leverage or were transferred to the Office of SBIC Liquidations.

One can also see in the chart above that for these years, leverage performance improved for funds licensed between 1999 and 2003, but appears to have declined for the funds licensed between 2004 and 2008. This may have been in part due to the overall economic decline in 2008. As shown previously in [Exhibit 3-3](#), SBIC performance generally follows the private equity industry and the stock markets.

Although the economy can impact SBIC performance, the most critical factor to keeping the program at zero subsidy cost is the underlying performance of each fund. The next section discusses underlying Debenture SBIC performance.

b. Debenture SBIC Performance

The table below shows the capitalization, distributions and residual values for Debenture SBICs licensed since 1998 by vintage year¹⁸ that issued Debenture SBIC leverage prior to 12/31/2012. Appendix B describes the methodology in developing the figures and metrics in this section.

Exhibit 6-4- Capitalization and Fund Value for Leveraged Debenture SBICs Vintage Years 1998-2012
As of 12/31/2012 (In \$ Millions)

Vintage Year	By Status				Capitalization					SBA	LP Distribution & Residual Value			
	Total	Liquidations	Surrender	Active	Private Committed Capital	Private Paid Capital	Leverage Issued	Total Capital Paid in or Issued	Weighted Interest & Annual Charge	Redemption, Interest, and Leverage fees	Private Net Distribution	Private Residual Value	Private Total Value	Private Total Value
1998	10	6	3	2	\$200.0	\$184.1	\$257.4	\$441.5	7.43%	\$301.2	\$119.1	\$40.1	\$40.1	\$158.2
1999	10	1	7	3	\$301.5	\$191.7	\$393.9	\$585.6	5.95%	\$518.9	\$321.7	\$123.2	\$123.2	\$444.8
2000	14	4	10	3	\$350.6	\$208.5	\$298.1	\$506.6	6.25%	\$365.0	\$307.3	\$93.9	\$93.9	\$401.2
2001	9	3	3	4	\$216.4	\$127.4	\$226.8	\$354.2	5.73%	\$278.5	\$136.6	\$70.2	\$70.2	\$206.8
2002	8	0	2	6	\$174.9	\$133.2	\$285.5	\$418.6	5.08%	\$212.7	\$177.0	\$115.9	\$115.9	\$292.9
2003	9	0	0	9	\$422.9	\$368.8	\$673.5	\$1,042.3	5.46%	\$543.7	\$423.1	\$275.9	\$275.9	\$699.1
20	4	0	0	4	\$128.4	\$103.4	\$195.1	\$298.5	5.96%	\$154.6	\$52.1	\$76.5	\$76.5	\$128.6
2005	9	0	1	8	\$365.6	\$278.9	\$486.1	\$765.0	5.84%	\$391.4	\$260.5	\$330.1	\$330.1	\$590.6
2006	12	1	0	12	\$585.7	\$482.1	\$927.8	\$1,409.9	5.37%	\$488.0	\$159.7	\$458.0	\$458.0	\$617.7
2007	8	0	0	8	\$518.6	\$405.6	\$692.4	\$1,098.0	4.52%	\$138.9	\$134.3	\$368.1	\$368.1	\$502.4
2008	7	0	0	7	\$256.5	\$206.1	\$371.4	\$577.5	4.14%	\$48.6	\$61.8	\$224.8	\$224.8	\$286.6
2009	9	0	0	9	\$534.3	\$333.1	\$587.3	\$920.4	3.65%	\$52.2	\$44.6	\$305.7	\$305.7	\$350.3
2010	20	0	0	20	\$1,153.0	\$697.6	\$1,207.6	\$1,905.2	3.51%	\$84.7	\$135.5	\$685.0	\$685.0	\$820.6
2011	18	0	0	18	\$1,202.7	\$551.4	\$782.9	\$1,334.3	3.31%	\$35.4	\$58.3	\$498.7	\$498.7	\$557.6
2012	18	0	0	18	\$813.1	\$291.2	\$259.5	\$550.7	3.45%	\$13.3	\$9.1	\$258.1	\$258.1	\$267.2
1998-2012	165	15	26	131	\$7,224.2	\$4,563.0	\$7,645.3	\$12,208.3	4.62%	\$3,627.2	\$2,399.7	\$3,924.2	\$3,924.2	\$6,323.9

Not surprisingly, fund distributions generally follow the same pattern as leverage repayment (Exhibit 6-3).

To assess how SBICs as a class perform to industry, Debenture SBIC pooled performance is benchmarked to the private equity industry. The exhibit on the next page compares pooled Debenture SBIC internal rate of return (IRR), total value to paid in capital (TVPI) and distributions to paid in capital (DPI) metrics to industry benchmarks by vintage year. As shown, although the Debenture SBIC unleveraged¹⁹ performance falls slightly below industry, the pooled private investor returns are commensurate with industry metrics due to the increase in leverage.

¹⁸ For the purposes of this report, the vintage year is defined as the calendar year in which the SBIC was licensed.

¹⁹ Unleveraged returns treat SBA leverage as part of private investor capital, in which draws are treated as paid in capital, and interest, charges, and redemptions are treated as private investor distributions. This helps SBA understand the value of leverage to the private investor and the underlying fund performance.

Exhibit 6-5- Comparison of Debenture SBIC Pooled Metrics to Private Equity Benchmarks by Vintage Year

Debenture SBIC Pooled Internal Rate of Return (IRR) by Vintage Year (n=100) As of December 31, 2012

	Year										
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Debenture SBIC Unleveraged	1.00%	11.30%	9.80%	6.70%	10.20%	9.90%	5.50%	11.30%	6.10%	6.90%	9.40%
Debenture SBIC Private Investor	-2.30%	16.10%	14.60%	9.10%	16.20%	14.70%	4.40%	17.00%	6.50%	8.00%	14.20%
Thomson Private Equity	5.80%	0.04%	6.05%	13.38%	15.03%	14.58%	11.09%	9.58%	4.17%	8.20%	13.11%
Prequin Private Equity	6.60%	4.60%	10.70%	17.20%	14.10%	15.60%	11.30%	6.70%	3.80%	7.90%	10.80%

Debenture SBIC Pooled Total Value Paid in Capital (TVPI) by vintage year (n=100) As of December 31, 2012

	Year										
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Debenture SBIC Unleveraged	1.05	1.68	1.53	1.38	1.50	1.47	1.29	1.53	1.22	1.16	1.20
Debenture SBIC Private Investor	0.86	2.32	1.92	1.62	2.20	1.90	1.24	2.12	1.28	1.24	1.39
Thomson Private Equity	1.35	1.00	1.36	1.68	1.69	1.67	1.54	1.50	1.18	1.27	1.34
Prequin Private Equity	1.34	1.30	1.56	1.74	1.61	1.69	1.57	1.35	1.21	1.26	1.29

Debenture SBIC Pooled Distributions to paid in Capital (DPI) by Vintage Year (n=100) As of December 31, 2012

	Year										
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Debenture SBIC Unleveraged	0.94	1.40	1.30	1.15	0.94	0.93	0.69	0.85	0.46	0.25	0.19
Debenture SBIC Private Investor	0.64	1.68	1.47	1.07	1.33	1.15	0.50	0.93	0.33	0.33	0.30
Thomson Private Equity	1.13	0.76	1.04	1.32	1.23	1.09	0.22	0.07	0.37	0.41	0.32
Prequin Private Equity	1.30	1.18	1.35	1.48	1.25	1.17	1.03	0.64	0.41	0.38	0.40

The prior chart demonstrates that Debenture leverage can significantly magnify private investor returns. How much returns are impacted depends on how much leverage the SBIC used and the SBIC's underlying performance. The chart below shows the impact on leverage performance by Prequin's Private Equity quartile.

Exhibit 6-6- Average Impact of SBA Debenture Leverage on Private IRR by Quartile For Debenture SBICs Licensed 1998 to 2008 as of 12/31/2012 (n=100)

Quarter (Q)	Unleveraged	Improvement	Decline	Average Private Investor IRR
1	20.10%	8.00%	-	28.07%
2	10.10%	5.20%		15.28%
3	5.10%	-	-0.80%	4.35%
4			n/m	Q4 Not meaningful (Avg. TVPI: 0.28)

As shown, SBICs in the top half of industry tend to benefit from SBA's leverage. However, SBA leverage tends to decrease returns for private investors in Debenture SBICs in the bottom half of industry. Not surprisingly, the break-even point coincides closely to the cost of SBIC leverage.

Exhibit 6-7- Unleveraged v. Private Investor IRR for Debenture SBICs with Positive Unleveraged IRR
Licensed 1998 to 2008 as of 12/31/2012 (n=83)

An analysis showed a regression on unleveraged versus private investor returns. The break-even point was approximately 5.7%, slightly higher than the dollar weighted cost of SBA leverage for these SBICs (5.5%).

Because SBICs are long term investments whose returns are realized over several years, another way to look at performance is horizon IRRs.

Exhibit 6-8- Comparison of Pooled Horizon Returns for Debenture SBICs Licensed 1998-2012 to Industry
As of December 31, 2012 (n=165)

	One Year	Three Year	Five year	Ten Year
Debenture SBICs -Unleveraged	10.00%	9.30%	7.50%	8.70%
Debenture SBICs - Private Investors	15.50%	14.70%	10.00%	12.90%
Preqin Private Equity	12.90%	13.50%	4.10%	17.90%
Thomson U.S. Private Equity	13.50%	11.00%	5.20%	9.50%
S & P 500 Index	16.20%	11.00%	2.93%	7.14%
Russell 2000 (U.S. small Cap) Index	16.40%	12.30%	3.56%	9.72%
Nasdaq Composite Index	16.30%	10.20%	4.00%	8.65%

As shown, Debenture SBIC performance has been comparable to industry, outperforming several industry benchmarks in the past five years. This may be due to improved licensing. The following chart shows the distribution of Debenture SBICs by Preqin Private Equity Quartile. The chart on the left shows the quartile based on the unleveraged performance and the chart on the right shows the quartile based on the private investor performance.

Exhibit 6-9- Debenture SBIC Quartile Distribution by Vintage Year
As of December 31, 2012

Distribution of Debenture SBIC Unleverage Performance by Preqin Private Quartile and Vintage Year for SBICs Licensed 1998-2007

Year	Quarter1	Quarter 2	Quarter 3	Quarter 4	n
1998-1999	15	10	40	35	20
2000-2001	4	26	39	30	23
2002-2003	12	29	47	12	17
2004-2005	23	31	38	8	13
2006-2007	5	60	30	5	20

Distribution of Debenture SBIC Private Investor Performance by Preqin Private Equity Quartile and Vintage Year for SBICs Licensed 1998-2007

Year	Quarter1	Quarter 2	Quarter 3	Quarter 4	n
1998-1999	25	5	15	55	20
2000-2001	13	26	26	35	23
2002-2003	29	18	35	18	17
2004-2005	31	23	23	23	13
2006-2007	40	25	25	10	20

The charts show that the percentage of Debenture SBICs in the bottom quartile has decreased, while the percentage in the top half has increased. Although undoubtedly beneficial to the private investors, this also yields benefits to SBA's leverage performance.

The following chart shows that all Debenture leverage losses for Debenture SBICs licensed between 1998 and 2008 have been from SBICs in the bottom quartile of private equity.

Exhibit 6-10- Leverage Status of Debenture SBICs by Preqin Private Equity Quartile for Vintage Years 1998-2008
As of December 31, 2012 (n=100)

	n	Repaid in Ops	Active	Transferred No Losses Anticipated	Transferred Losses Realized or Anticipated
Quarter 1	10	40%	60%	0%	0%
Quarter 2	33	24%	76%	0%	0%
Quarter 3	38	39%	58%	3%	0%
Quarter 4	19	5%	16%	37%	42%

Not surprisingly, over three quarters of the bottom quartile performers have been transferred to Liquidations. In analyzing its portfolio, SBA has noticed two key characteristics which may be related to performance: **fund size** in terms of how much private capital was raised and **strategy**.

The next chart compares the pooled IRRs based on fund size (measured by the amount of private capital raised by the SBICs and indexed from the date of licensing to calendar year 2013).

Exhibit 6-51- Pooled IRRs by Fund Size* for Debenture SBICs Licensed 1998 to 2008
As of December 31, 2012 (n=100)

	Unleveraged Pooled IRR	Private Investors Pooled IRR
\$25 Million +	9.40%	13.70%
Under \$25 Million	2.50%	0.80%
All SBICs	8.10%	11.00%

* Fund Size is based solely on private capital and determined by the highest regulatory capital reported on annual form 468s and indexed from the SBIC's licensing date to CY 2013.

As shown in the chart above, SBICs that raised more private capital had higher returns for its investors than those that raised less money.

The following exhibit compares Debenture SBICs by strategy. Although SBICs with buyout/hybrid strategies have generally performed better, there have been fewer SBICs to observe.

Exhibit 6-62- Distribution of IRRs by Strategy for Debenture SBICs Licensed 1998 to 2008
as of December 31, 2012

**Distribution of Unleveraged IRRs by Strategy for Debenture SBICs Licensed
1998 to 2008 as of December 31, 2012**

	Buyouts/Hybrid Strategy	Mezzanine
Negative	7%	20%
0 to 6%	25%	24%
6 to 8.99%	25%	29%
9 to 11.99%	4%	17%
12 to 18%	18%	11%
Over 18%	21%	0%

**Distribution of Private Investors IRRs by Strategy for Debenture SBICs Licensed
1998 to 2008 as of December 31, 2012**

	Buyouts/Hybrid Strategy	Mezzanine
Negative	11%	30%
0 to 6%	18%	18%
6 to 8.99%	14%	5%
9 to 11.99%	11%	15%
12 to 18%	7%	21%
Over 18%	39%	11%

Appendix A. Data Sources and Methodology

The analyses and exhibits used throughout these reports were derived primarily from data provided by the Data Management Division of SBA's Office of Investment and Innovation. Data Management collects and reports both internal and external data, including general SBIC information, funding data, processing metrics, SBIC financings, reported SBIC financial information and recovery data from the Office of SBIC Liquidations. Much of the information identified in this report may be found in table format in the quarterly report published by Data Management on the SBA website at:

<http://www.sba.gov/content/quarterly-sbic-program-statistics-0>.

The table below maps the data sets used in each of the exhibits in the report. As noted below, some exhibits are derived from multiple data sets.

Data Set	Exhibits
SBIC Directory Information (table tblDirectory) – Contains general SBIC information for Operating SBICs, including private capital, SBA guaranteed leverage, and licensing date. Data Management keeps data as of the end of each government fiscal year.	3-1; 3-2; 3-4; 4-1; 5-8; 6-2
SBIC Performance Metrics - SBIC performance metrics are estimated from SBIC reported data as well as recovery data from the Office of SBIC Liquidations. More information regarding this information may be found in Appendix B.	3-3; 6-4; 6-5; 6-6; 6-7; 6-8; 6-9; 6-10; 6-11; 6-12
Debenture Trust Certificate data located at http://www.sba.gov/content/trust-certificate-rates-annual-charge-debenture-program .	3-5
SBIC Financing Form Information (table tblForm1031) – Contains SBIC finances data as reported by the SBIC on Form 1031.	3-6; 4-1; 4-2; 4-3; 4-4; 4-5; 4-6; 4-7; 4-8; 4-9;
September 30, 2013 Quarterly Report at http://www.sba.gov/sites/default/files/files/WebSBICProgramOverview_September2013.pdf	4-10; 5-3; 5-4; 5-5; 5-7; 5-9; 5-10; 6-1; 6-2
SBIC History Information (table tblDirectoryHistory) – Contains general information on SBICs licensed both operating and inactive, including initial capital at licensing, licensing date, and status.	5-6; 6-3
Funding tables – This consists of the SBIC commitment and ten year debenture tables.	6-3
Capital Impairment Data – Updated from last annual report with data from Operations	6-2
Thomson One Private Equity Data – SBA downloads financing and performance information from Thomson One (http://thomsonone.com) in order to compare the SBIC program as a class to other U.S. private equity financings and private equity fund performance. Thomson One also provides performance benchmarks for the S&P 500, Russell 2000, and NASDAQ composite index.	3-3; 6-5; 6-8
Preqin Private Equity Performance Data – SBA downloaded performance benchmarks for Private Equity from Preqin (http://www.preqin.com/) in order to compare SBIC performance to the private equity industry as tracked by Preqin. SBA identifies SBIC quartile performance based on Preqin Private Equity benchmarks.	3-3; 6-6; 6-8; 6-9; 6-10

Appendix B - SBIC Performance Metrics

This appendix describes the data and assumptions for computing SBIC performance metrics as of December 31, 2012 for SBICs licensed since 1998 that issued Debenture leverage only. SBA estimated SBIC performance metrics, using data reported by SBICs on Form 468s (SBIC Annual Financial Report) and the Office of SBIC Liquidations Ultimate Loss reports. As a disclaimer, no audits or peer reviews were performed on any of these calculations. Private investors interested in the program should perform their own due diligence and analysis in evaluating individual funds or the risk associated with SBICs.

These metrics exclude SBICs that did not issue Debenture leverage prior to December 31, 2011 or issued preferred stock or participating securities at some time. SBICs licensed prior to 1998 are not included due to data limitations.

SBA calculates both returns to the private investor and unleveraged returns. Unleveraged returns treat SBA leverage as part of private investor capital, in which draws are treated as paid in capital, and interest, charges, and redemptions are treated as private investor distributions. This helps SBA understand the value of leverage to the private investor and the underlying fund performance.

SBA is only able to estimate all return data since individual fund waterfall terms and conditions (such as hurdle rates and carried interest) vary from fund to fund. In addition, in some funds waterfall terms may differ for key investors.

SBA uses SBIC reported Form 468s (Annual Financial Reporting) and the Office of Liquidation's fiscal year end Ultimate Loss Reports for fiscal years 2002 through 2013 to estimate cash flows, asset values, and performance metrics. (The first SBIC transferred to the Office of SBIC Liquidations for this population was in fiscal year 2002).

SBA's estimated performance may differ from actual performance for a number of reasons, including:

- **Waterfall:** The waterfall may be different for the SBIC. Some SBICs have hurdle rates not considered by SBA calculations which would improve the performance to the private investor in profitable funds. SBA's calculations assume that all SBICs have the same waterfall terms as follows:
 - All calculations are net of fund expenses and carried interest.
 - SBIC managers receive a 20% carried interest after investors receive cumulative distributions equal to cumulative paid-in capital.
 - SBA assumes there is no hurdle rate.
- **Annual Versus Monthly Cash flows:** Due to data limitations, SBA only uses annual cash flows versus monthly cash flows typically used by benchmarking services.
- **Valuations:** SBICs typically utilize SBA Valuation Guidelines to value their portfolio versus Generally Accepted Accounting Principles (GAAP).
- **Data Sources Have Different Timing:** The Office of Liquidation's fiscal year end is September 30th while most SBIC annual financial reports are December 31st.
- **Lack of Form 468 Data for SBICs Transferred to the Office of Liquidations:** Not all SBICs continue to report Form 468 information after being transferred to the Office of Liquidation. In these instances, the last reported Form 468 was used. Since the Office of Liquidation's report is used to capture SBA cash flows and residual value, these only impacts return calculations for SBICs that repay all SBA leverage in full.

- **Missing Private Investor Information:** SBA uses cumulative private investor paid in capital and cumulative private total distributions reported as the primary means of capturing private investor cash flows. These fields were not added until fiscal year 2007. In addition, many SBICs did not complete these fields even after they were added to the form. When these fields are not completed, SBA uses the cash flows identified as reported on the Statement of Partners Capital on the Form 468. This statement is used versus the cash flow statement because the Statement of Partners Capital checks to ensure the cash inflows and outflows match the balance sheet. In a few cases, SBICs may have recorded transfers of partnership interests within these pages which may cause slight variations in some of the performance calculations. The cumulative private investor fields obviate problems with transferred interests. The new web-based system is expected to mandate these fields to better capture this data.
- **Starting Point:** SBA is only able to capture information from the first Form 468. In some cases, SBA may be missing the first year of cash flows for the fund. SBA assumes that the contributed capital represents the first cash flow.
- **SBIC Surrenders:** Once a fund repays SBA its guaranteed leverage and surrenders its license, SBA is no longer able to report performance. SBA reports the last observed metrics for Surrendered SBICs. In some cases, the Form 468 data may not contain a cash flow showing the SBIC repaid its leverage. In these cases, SBA assumes that all surrendered SBICs repay leverage in the year it surrendered. In addition, since SBICs may have made distributions to private investors post surrender, DPI metrics may be understated and other performance metrics may differ from actual performance.

SBA calculates four basic performance metrics for each SBIC in the population from both a private investor perspective and unleveraged performance perspective minus expenses and an assumed 20% carried interest after the private investor receives distributions equivalent to paid in capital as follows:

- **Distributions to Paid in Capital (DPI):** This is calculated by summing all relevant distributions minus any carried interest and dividing by the sum of all paid in capital.
- **Residual Value to Paid in Capital (RVPI):** This is calculated by taking the net asset value minus any forecast carried interest and dividing by the sum of all paid in capital.
- **Total Value to Paid in Capital (TVPI):** This is calculated as the sum of DPI and RVPI and represents the overall multiple.
- **Internal Rate of Return (IRR):** This represents the discount rate that equates the net present value of the SBIC's net cash flows.

SBA also calculates pooled metrics by vintage year and across vintage years (first year SBIC reported its Form 468). Pooled metrics aggregate cash flows from all funds to calculate the above metrics. Pooled metrics help to compare the SBIC as a class to comparable industry metrics.

SBA also calculates pooled horizon returns for its SBICs. Horizon IRRs are calculated using funds' net asset values as a negative outflow at the beginning of the period, with any distributions during the period and the funds' residual values used as a positive inflow at the end of the period. Horizon IRRs are dollar-weighted and net of management fees and carried interest.