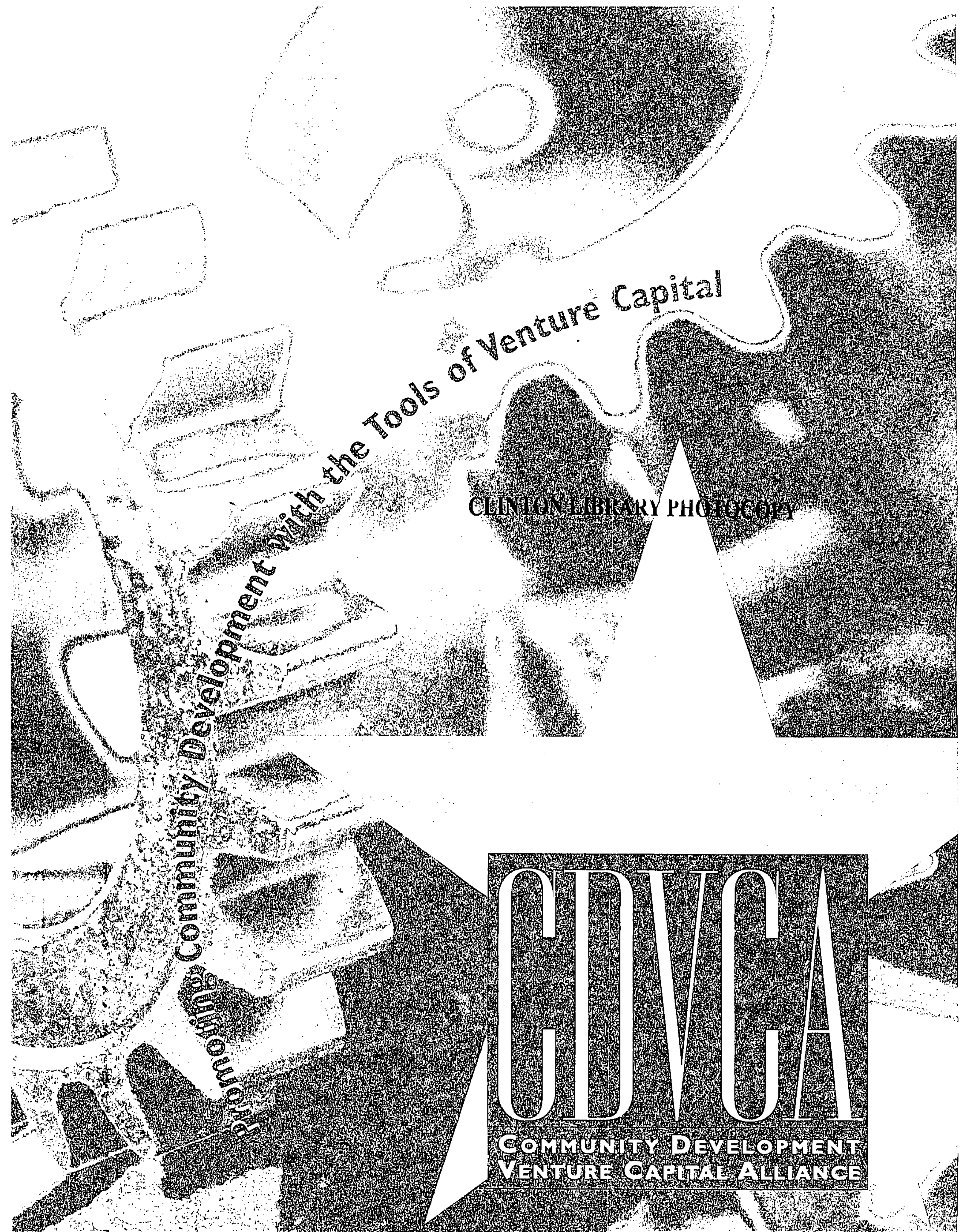

Promoting Community Development with the Tools of Venture Capital

CDVCA

COMMUNITY DEVELOPMENT VENTURE CAPITAL ALLIANCE

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Ventures

Promoting Community Development with the Tools of Venture Capital

Vol. 2 No. 1
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Community Development Venture Capital Alliance

CDVCA Enters a New Era

Community Development Venture Capital Alliance (CDVCA) has instituted a series of organizational changes that will position the association to play a central role in building the field of community development venture capital. According to CDVCA Chairman, Nick Smith, these changes, which include the hiring of a full-time staff and the relocation of CDVCA's headquarters to New York City, will enable CDVCA to respond effectively to the rapidly growing needs and demands of the field.

"Since 1992, an extremely active group of dedicated members, volunteers and consultants has enabled CDVCA to play a key role in promoting one of the most promising models currently used in community development finance," said Mr. Smith. "We have demonstrated that there is a significant and growing need for our services. And we have decided that it is time we had a professional staff to meet those increasing demands. As a result, our members will see a significant expansion of services, particularly in the areas of training, technical assistance and access to funding."

> "Changes at CDVCA mean that we can have a more lasting impact on the field."
>
> Nick Smith,
> CDVCA Chairman

As part of the restructuring, the CDVCA board of directors has named Kerwin Tesdell to be the organization's first full-time president. Formerly a program officer for the Ford Foundation's Economic Development unit, Mr. Tesdell assumed this position in February 1998. (See profile on p.2) Meg Barnette, a Skadden Fellow funded by the law firm Skadden Arps, also joined the staff in February and will stay on as a staff member after her fellowship ends. Although the full-time staff is expected to expand as necessary, Mr. Smith anticipates that members and volunteers will remain actively involved. "If anything, I think their involvement will increase as more opportunities arise and as the staff has a better ability to follow through," said Mr. Smith.

"With the addition of our new staff, we're going to be able to work more effectively with angels and traditional venture capitalists. And that will be a big advance-

Continued on page 2

Letter from the President

It is a pleasure to write my first letter in *Ventures*, as CDVCA's new president. So far, the job has been great. I am privileged to work daily with people who combine extraordinary skills and abilities with dedication to community and a strong sense of economic justice. Our board, membership, and staff are populated with great people who work hard and care deeply about what they do. I couldn't ask for better or more inspiring colleagues.

Also, it has been quite an experience to be on the other end of CDVCA's phone for the past six months, hearing about all the innovative efforts developing around the country and around the world to find ways to use the discipline of business investment to build healthier communities.

Continued on page 2

Please Join Us

Meet us in Philadelphia for Our Biggest Annual Conference Ever

CDVCA's Annual Conference
December 1 - 3
Philadelphia, PA

for details see back page

Northeast Ventures

REMARKS BY NICK SMITH, CHAIRMAN,
NORTHEAST VENTURES CORPORATION
United States Senate Small Business Committee Policy Roundtable

May 12, 1999

Members of the Committee on Small Business
United States Senate, SR-428
Washington, DC 20510

Dear Mr. Chairman and Senator Kerry:

Thank you for the opportunity to participate in today's roundtable policy discussion and to submit this letter for the Committee's record. I am Nick Smith, Chairman of Northeast Ventures Corporation of Duluth, Minnesota. Northeast Ventures is a community development venture capital fund and a certified community development financial institution (CDFI).

In addition to thanking the Chairman and the Ranking Member, I also would like to greet my own Senator, Paul Wellstone of Minnesota. Senator Wellstone is a Member of this Committee and has served our state's small business community extremely well. It has been a pleasure to work with him on the issue I am here to discuss today, community development venture capital.

I am proud to have worked with the Senator on a number of additional issues affecting the economy of my home area, which is the Northeastern part of Minnesota, including the North Shore of Lake Superior and the state's famous Iron Range region. It is a mainly rural region which has seen boom and bust, and which continues to have tremendous untapped economic potential. That is the mission of Northeast Ventures – to promote the diversification and strengthening of Northeastern Minnesota's economic base.

I am here today as Chairman and CEO of Northeast Ventures Corporation. I also serve as Chairman of the Community Development Venture Capital Alliance.

My comments today, here and during discussion, will focus on an exciting new field of enterprise. Northeast Ventures is part of an industry which we call the community development venture capital industry. It is made up of venture capital funds throughout the country. These funds have the mission and the capacity to provide developmental venture capital effectively, to generate entrepreneurial capacity, and to create jobs and wealth in low-income areas. According to the most recent published material I have seen on the subject, there are over 40 such funds in the United States, with something over $330 million under their management.

The industry combines disciplined equity investment with intensive entrepreneurial and managerial assistance to help businesses form and prosper in economically distressed areas. Community development venture capitalists believe in a "double bottom line" of social and financial objectives. Those dual objectives are the purpose of our work as companies and organizations. They are our mission.

In our industry, we believe we have begun to establish a strong record of effectively providing equity financing in a disciplined way to growth firms in economically distressed urban and rural areas. We are proud and excited that some of our initial successes are beginning to receive positive recognition. I believe today's roundtable and the President's event yesterday in Atlanta are illustrations of the fact that we are on to something. I think we are on to the next wave of important social and economic innovation in the United States.

Before talking about what I am sure the Committee is interested in, which is federal legislative ideas, let me just mention some principles and practices at Northeast Ventures that I believe help illuminate what the community development venture capital funds do.

Northeast Ventures operates in a manner that:

- demonstrates commitment to the social component of the corporation's mission;
- achieves permanence through financial self-sufficiency;
- reflects and fosters innovation and effectiveness in a results-oriented environment; and
- establishes the organization as a leader in rural economic development at the regional, state and national level.

Managerially, Northeast Ventures:

- maintains an investment portfolio diversified by industry sector, development phase, investment structure and geography;
- evaluates each opportunity according to its compatibility with corporate social goals, its growth potential, its product, market and competition, its management and its financing requirements;
- uses an intensive and thorough, but flexible, due-diligence process;
- does not invest more than 10 percent of its capitalization in any single opportunity, to limit exposure to risk;
- actively monitors all portfolio companies according to the need of each company and to its own corporate objectives;
- takes a conservative approach to portfolio valuation to ensure long-term viability; and

- exits investments in such a way as to achieve an optimal rate of return at the earliest possible date, without sacrificing long-term prospects for the company or its location in the region.

We in the community development venture capital industry believe we are doing well. We also believe we are doing good, and we believe that our mostly local examples could blossom into something much larger. We believe that with modest federal government assistance, tremendous benefits could be delivered in economically distressed areas.

This Committee has jurisdiction over programs administered by the SBA. Therefore, I would like to mention two proposals which really promote the same idea – both of which are ideas for new SBA activities. Senator Wellstone has introduced a bill, S. 619, the Community Development Venture Capital Assistance Act of 1999. It is the same as the bill which passed both in this Committee and in the full Senate last year as part of larger legislation. The other proposal, of course, is the New Markets Venture Capital Companies (NMVCs) proposal, included in the President's FY 2000 Budget request as a new SBA program.

I support both proposals and believe they are complementary. I am very encouraged that the President has requested a total of $45 million to carry out a NMVCs program. And I would be very pleased to work with the Committee to try to find a way to authorize a workable program that achieves the aims of both the Administration and the Wellstone proposals. Others can discuss details of these ideas, and I am willing to do so, as well. But I will close my initial remarks at this point, and I thank the Committee for its attention.

Sincerely,

Nick Smith

Nick Smith,
Chairman, Northeast Ventures Corporation

The Double

By Kerwin Tesdell, President, Communi
Julia Rubin, Doctoral Candidate, Organiz

Kentucky Highlands Investment Corporation has worked for thirty-two years to alleviate poverty in the heart of Appalachia. In Duluth, Minnesota, Northeast Ventures has spent a decade tackling the economic devastation brought on by dramatic reductions in the region's ore mining industry. In 1996, Boston Community Ventures was established in one of the poorest sections of Boston to foster the creation of quality jobs and the growth of socially responsible businesses. Meanwhile, similar efforts have sprung up in such diverse locations around the world as Nizhny Novgorod, Russia; Zagreb, Croatia; and Lima, Peru.

What do these organizations have in common? They are all community development venture capital (CDVC) funds, members of a new but rapidly growing field of organizations that use the tools of venture capital to create good jobs, productive wealth, and entrepreneurial capacity to benefit disadvantaged people and economically distressed communities. They seek to apply the powerful engine of growth that has driven the economic expansion in Silicon Valley, and other hotbeds of business development, to communities that the current prosperity has passed by.

CDVC funds make equity and equity-like investments in highly competitive small businesses that hold the promise of rapid growth. These fast growing companies produce a "double bottom line" of not only financial returns, but also social benefits in the form of good jobs and healthier communities. The investments typically range from $100,000 to $1 million, much smaller than most traditional venture capital investments.

The companies in which CDVC funds invest generally employ between ten and one hundred people. Investors in CDVC funds include foundations, banks, insurance companies and other corporations, government, and private individuals. They invest because of an interest in the social and financial returns of the funds; they too are interested in the double bottom line.

The CDVC Industry

There are currently more than forty CDVC funds operating across the United States and Canada. In the U.S. alone, such funds have more than $330 million under management. CDVC funds have also become a powerful economic development tool in economies in transition in Eastern Europe and in developing economies in Latin America.

CDVC funds come in many different forms, including not-for-profit, for-profit, and quasi-public organizations. Their structures encompass for-profit "C" corporations, limited partnerships, limited liability companies, community development corporations (CDCs), and Small Business Investment Companies (SBICs). Despite this structural diversity, CDVC funds all share a commitment to the creation of good jobs through business investment.

CDVC funds use a multitude of investment techniques to accomplish their missions. These range from the purchase of preferred and common stock to the provision of subordinated debt with equity "kickers" such as warrants or royalties. CDVC funds, as compared with lenders, thus structure their financing so that they enjoy the "upside" when a company does well, but also the "downside" when a company does poorly. For this reason, CDVC funds take a much more active role than a lender ever would in advising, and sometimes even helping manage, an investee's business, in order to help it succeed and grow rapidly. This often-intensive entrepreneurial and managerial assistance is the heart of the economic development impact of CDVC.

Why Community Development Venture Capital?

There are a number of reasons that community development venture capital is a powerful tool for economic development.

➤ Equity capital is vital to the success and growth of small businesses, particularly during their expansion stage when large numbers of jobs and productive wealth are being created. Because equity capital is high risk, it is very difficult to access.

➤ Equity capital is in particularly short supply in low-income areas and among minority entrepreneurs. The primary source of risk capital for most small businesses is personal savings and loans from friends and family. In low-income areas, these tend to be lacking. Traditional venture capital firms provide financing for only a tiny portion of businesses nationally, and venture capital is almost completely absent from low-income urban and rural areas.

ENT VENTURE CAPITAL

Frank Serr

Bottom Line

evelopment Venture Capital Alliance and
onal Behavior Program, Harvard University

➤ Equity capital leverages other financing. Banks and other lenders will not make loans to businesses unless they maintain a prudent ratio of equity to debt capital. An infusion of equity capital is often the linch pin for assembling other financing for new or expanding businesses.

➤ CDVC funds target companies that are highly competitive and thus likely to expand rapidly. These companies not only provide substantial financial returns, they also create large numbers of good jobs and have the financial resources to offer decent wages, employee benefits, worker training, and opportunities for career advancement. This sector of small, competitive businesses can form the backbone of a successful local economy.

➤ CDVC funds provide significant entrepreneurial and managerial assistance to businesses. Unlike lenders, equity investors become partners with their investee companies, sitting on their boards of directors and providing other substantial assistance by identifying additional financing, making contacts with customers and suppliers, and helping with executive recruitment. For businesses in low-income areas, this assistance is often as crucial as the financing itself.

➤ Some CDVC funds operate, or have relationships with, workforce development programs that help place unemployed people in jobs that are created by their financing activities.

➤ Some CDVC funds go beyond providing financing and technical assistance to existing businesses. They start and nurture businesses, and then recruit local business people to own and operate them. In this way, CDVC funds are able to jump-start business development in even the most economically distressed areas.

The Difficulties of the Double Bottom Line

A focus on social returns differentiates CDVC funds from traditional venture capital funds. Like traditional venture funds, however, CDVC funds must also deliver financially to remain in operation. This double bottom line of social and financial objectives presents many challenges that are different from those that traditional venture capital funds encounter. Among the challenges that the CDVC industry faces are problems in raising capital and reaching scale, difficulties in attracting experienced talent, and high costs of operation.

Problems In Raising Capital and Reaching Scale

The pool of potential investors that share an interest in the social component of the double bottom line is limited, and CDVC funds generally do not offer traditional venture capital returns. For this reason, CDVC funds find it difficult to raise large amounts

> *“CDVC funds use a multitude of investment techniques to accomplish their missions. These range from the purchase of preferred and common stock to the provision of subordinated debt with equity “kickers” such as warrants or royalties.”*

The Community Development Venture Capital Alliance (CDVCA) promotes use of the tools of venture capital to create good jobs, productive wealth, and entrepreneurial capacity that benefit low-income people and distressed communities. CDVCA's members operate funds in low-income urban and rural areas throughout the United States and around the world. It seeks to build the field of community development venture capital by providing training, offering opportunities for peer exchange and learning, increasing members' access to capital and other resources, providing individualized consulting services, developing standards and best practices, and advocating for the field. It also encourages and facilitates involvement of the traditional venture capital communities in community development finance.

About the Author

Julia S. Rubin is a doctoral candidate in Harvard University's Organizational Behavior Program. Her dissertation examines the field of community development venture capital.

Formerly, Ms. Rubin consulted for McKinsey & Company and worked in brand management for Procter & Gamble and Eastman Kodak. She received her M.B.A., M.A. and B.A. degrees from Harvard University.

About the Author

Kerwin Tesdell is president of the Community Development Venture Capital Alliance and also an adjunct professor at New York University School of Law.

Formerly, Mr. Tesdell was a program officer at the Ford Foundation and director of the Community Development Legal Assistance Center in New York. He holds an economics degree from Harvard College, law and business degrees from New York University, and a certificate from the Venture Capital Institute.

of capital, and the average size of a mature CDVC fund in 1996 was only \$5.8 million. This is significantly smaller than most traditional venture funds, and also less than the approximately \$10 million minimum generally thought necessary to help cover operating expenses, attract experienced fund managers and allow for investment diversification. Substantial new sources of risk capital must be found for funds in the CDVC industry to reach an economic scale where the full power of the model may be demonstrated.

Attracting Experienced Talent

Only a small number of individuals have the skills necessary to operate a successful equity investment program. Most of them work for traditional venture funds and are highly compensated for their work. Those with the necessary skills and experience to produce the double bottom line of making successful financial investments while also creating social benefits are even more scarce. The relatively small number of CDVC funds currently operating has thus far been fortunate in attracting extraordinarily talented and dedicated people. Creating opportunities for training and apprenticeship learning will be necessary to allow the CDVC industry to continue its rapid expansion and retain its high quality.

Costs of Operation

The economics of CDVC funds are fundamentally different from those of traditional venture capital funds: CDVC funds are generally more expensive to operate, as a percentage of funds under management. Increased scale would help this problem, but, for at least two reasons, costs will always remain an issue. First, the size of the average CDVC investment is significantly smaller than that of the average traditional venture investment, although the cost of making a smaller investment is often as great as making a larger one. Also, CDVC funds often become even more involved in providing entrepreneurial and managerial assistance to their investee businesses than do traditional venture capitalists, and this too is expensive. The smaller investment size and greater business assistance are both integral to achieving the social benefits of CDVC funds. For investment returns not to be unduly reduced, a model must be developed that will help pay for the social benefits produced by CDVC funds from a source other than investment earnings alone.

Future of the Industry

Economic development professionals, as well as leaders in finance and business, are increasingly turning to CDVC as an effective way to help build healthy communities and make durable improvements in the lives of disadvantaged people. While CDVC shows great promise, the jury is still out regarding the full measure of its effectiveness. As existing funds mature and newer ones are formed, they are sharing knowledge and best practices with each other, and efforts are under way to measure the full social benefit and financial returns of the industry. Together, these funds are experimenting with and building a model that is different from traditional community economic development, but is not quite venture capital either. It is a new hybrid that borrows sophisticated tools of finance and business development and applies them in promising new ways to some of the most serious and intractable problems of our time. ***CI***

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Venture Capital for Community Development in New Markets – Draft, 6-99

With 17.7 million new jobs created in the United States since 1993, there is no question that our national economy is experiencing extraordinary growth. Unfortunately, the prosperity created by our strong economy and enjoyed by most Americans today has not been shared by many people living in low-income urban and rural communities. This inequity exists, in part, because many of the poorest regions of our country have been unable to attract the equity capital and technical assistance that is the key to starting and expanding businesses.

In recent years, a new industry of community development venture capital funds has emerged to help people in our poorest communities experience the full impact of this robust economy. Community development venture capital funds (CDVCs) apply the tools of venture capital to fuel business creation and expansion, create good jobs and improve the lives of people in economically distressed communities. These funds seek to demonstrate that the same model of business development that has driven the economic expansion in regions like the Silicon Valley and Route 128 in Massachusetts can also make a powerful difference in areas like the Mississippi Delta, inner-city Baltimore, and Appalachia. There are currently more than 40 CDVC funds operating and fund-raising across the United States and Canada. In the U.S. alone, such funds have nearly $300 million under management.

In the heart of Appalachia...*Kentucky Highlands Investment Corporation (KHIC)* *invests in start-up and expanding businesses located in Southeastern Kentucky, but it has also been responsible for creating successful new businesses from the ground-up. If it recognizes a serious market need, KHIC leadership will write -- and finance -- a business plan, recruit a CEO to run the business, and provide ongoing management assistance to ensure its success. Several thriving businesses have been created in this way by Kentucky Highlands.*

In inner-city Baltimore...*Community Development Ventures, Inc. (CDV)* *is providing equity financing to businesses that are in need of growth or start-up capital in and around Baltimore's Empowerment and Enterprise Zones. CDV, which has raised a total of $8 million in its first year, also offers a Management & Technical Assistance Program to Baltimore businesses and a Youth Entrepreneurial Program that promotes entrepreneurial awareness and skills among high school students.*

In Northeastern Minnesota...*where the restructuring of the U.S. steel industry has devastated the region,* ***Northeast Ventures*** *was created in 1989 for the explicit purpose of jump-starting the region's economy. Since then, Northeast has invested a total of $8.3 million in 23 local businesses, creating or saving nearly 700 jobs. NEV fund managers become intensely involved in the day-to-day operations of each portfolio company, providing advice and assistance on virtually every phase of the business, including board development, executive recruitment, financing, marketing and strategic planning.*

Although these funds are committed to a "double bottom-line" that considers both the social and financial implications of their investments, community development venture capital funds conduct the same rigorous analysis that any traditional investor would. They are commited to fighting poverty, but they are in every way serious investors who invest in companies with strong management, good ideas, impressive growth potential, and the promise of high return rates. These mission-driven funds are demonstrating that there are potential business opportunities -- with tremendous social benefits -- in rural and inner-city communities. However, many of these businesses need the kind of intensive nurturing that most traditional investors are not willing to provide and that community development venture capital funds consider central to their work.

Two new initiatives that will be considered by the 106th Congress this year build on the promise of these community development venture capital funds and look to public/private cooperation to support their work and increase the flow of capital into traditionally underserved areas and populations. The **New Markets Venture Capital Program**, proposed by President Clinton in his budget proposal for FY 2000, would create 10-20 New Markets Venture Capital Companies (NMVCs) to provide a combination of equity venture capital financing and technical assistance to smaller businesses located in low- and moderate income areas. And the **Community Development Venture Capital Assistance Act of 1999** (S.619), which was passed by the Senate last year and has been reintroduced by Senator Paul Wellstone this year, would provide matching funds to strengthen and support this emerging field through professional training programs, internships, technical assistance, research activities, and promotion of best practices. These two pieces of legislation complement each other and, together, will help build a strong industry of funds that will serve distressed communities throughout the country.

Addressing the Key Needs of the Field: Equity Capital, Technical Assistance and Capacity Building

The emerging community development venture capital industry has demonstrated that it can be a powerful tool for economic development and community revitalization, but to achieve its full potential, it will need the increased public and private support that the New Markets Venture Capital Program and the Community Development Venture Capital Assistance Act of 1999 can provide. These programs address the three most critical needs of the field: equity capital, technical assistance and industry capacity building.

Equity Capital and Technical Assistance: Inextricably Linked

The New Markets Venture Capital (NMVC) program would create 10-20 New Markets Venture Capital Companies (NMVCs) to provide a combination of equity venture capital financing and technical assistance to smaller businesses located in low- and moderate-income areas. The program, which will be administered by the U.S. Small Business Administration (SBA), will fill equity-financing needs not currently being met through existing public or private financing programs and will complement the SBA's existing equity investment program.

To significantly increase the supply of equity available to low- and moderate-income communities, the SBA studied the community development venture capital industry, whose members have been making successful equity investments in these areas, and used the CDVC model to formulate the New Markets Venture Capital program.

NMVC Program Structure

The New Markets Venture Capital program would allow participating funds to receive up to $10 million in matching equity capital and up to $3 million in matching technical assistance funding. Participation would be on a competitive basis and would be geared toward funds with a combination of a strong financial track record and a mission of community development.

NMVCs will be newly-formed for-profit venture capital investment companies. Unlike SBICs, NMVCs will not be licensed by SBA. Instead, SBA will enter into an agreement with each NMVC, setting forth the specific terms of that firm's participation in the program. Each NMVC would be eligible for SBA-issued Debentures, which will have deferred interest for the first five years of a ten-year term. The NMVC structure will allow the SBA to leverage government guaranteed funding through the matching capital raised by an NMVC to produce the maximum amount each NMVC can offer in LMI Investments. The NMVC program will be community-based to specifically meet the needs of the area in which it operates.

Capacity Building: Boosting the Benefits of A New Industry

Passed by the Senate last year, and reintroduced in the Senate this year by Senator Paul Wellstone of Minnesota, the **Community Development Venture Capital Assistance Act of 1999** would promote the development of community development venture capital organizations by providing matching funds for a range of "capacity building" activities for the industry, including professional training programs, internships, technical assistance, research activities, and promotion of best practices.

Program Structure

This legislation would provide $20 million in matching funds over four years to build and strengthen the field of community development venture capital through a number of activities. The legislation would authorize the U.S. Small Business Administration to enter into contracts with and make grants to intermediary organizations and community development venture capital funds and would enhance the economic development benefits of the industry by:

- Enhancing the professional skills of professionals in the field through training programs, university centers, and internship opportunities.

- Promoting best practices in the field through conferences, publications, and networking opportunities.

- Supporting research on economic, operational, and policy issues relating to community development venture capital.

- Providing for intense, direct assistance to strengthen and support community development venture capital funds.

# # #

Q & A

Q: How does community development venture capital benefit distressed communities?

A: First, it provides access to the equity capital that is vital to the success and growth of small businesses and is in particularly short supply in low-income areas. The primary source of risk capital for most small businesses is personal savings and loans from friends and family. In low-income areas, these tend to be lacking. Traditional venture capital firms provide financing for only a tiny portion of businesses nationally, and venture capital is almost completely absent from low-income urban and rural areas. Equity capital also leverages other financing. Banks and other lenders will not make loans to businesses unless they maintain a prudent ratio of equity capital to debt capital. An infusion of equity capital is often the linchpin for assembling other financing for new or expanding businesses.

Second, CDVC funds target companies that are highly competitive and likely to expand rapidly. These companies not only provide substantial financial returns, they also create large numbers of good jobs and have the financial resources to offer decent wages, employee benefits, worker training, and opportunities for career advancement. This sector of small, competitive businesses can form the backbone of a successful local economy.

Third, CDVC funds provide significant entrepreneurial and managerial assistance to businesses. Unlike lenders, equity investors become partners with their investee companies, sitting on their boards of directors and providing other substantial assistance. For businesses in low-income areas, this assistance is often as crucial as the financing itself. In fact, some CDVC funds go beyond providing financing and technical assistance and actually start and nurture new businesses, and then recruit local business people to own and operate them. In this way, CDVC funds are able to jump-start business development in even the most economically distressed areas.

Q: Why do CDVCs need help raising equity capital?

A: Because their developmental mission calls for them to focus their investments in low-income regions, community development venture capital funds are not able to reach the same "economies of scale" as traditional venture capital funds. CDVCs work on smaller deals and provide more technical assistance than traditional venture capital funds, which significantly raises the cost of operation for the equity fund. As a result, CDVC funds can sometimes have a difficult time raising enough capital to begin investing and to cover their higher operating expenses. While traditional venture capital funds' overhead rarely exceeds 2.5 percent of assets, CDVCs' overhead can be as high as 8 or 9 percent.

The New Markets Venture Capital program is designed to help remedy this lack of equity capital by making it easier for developmental venture capital funds to become economically viable. By providing matching capital in the form of a zero coupon debenture and matching technical assistance in the form of a grant, the NMVC program will enable many more developmental venture capital funds to reach scale and begin investing. This will dramatically increase the supply of equity capital in low and moderate-income areas, fostering new business growth and job creation.

Q: Can't existing small business assistance programs address the needs outlined in the NMVC Program?

A: The New Markets Venture Capital Program is designed to complement the SBA's existing programs and represents a new model of small business development that is unique in almost every way. CDVC funds are mission-driven investment funds that make it their work to operate in low-income communities, invest in new or expanding businesses for the purpose of creating jobs, and roll up their sleeves to do everything possible to make those businesses succeed. When they invest in a business, they commit to a long-term partnership with the entrepreneur. That often means doing everything from helping an entrepreneur develop a business plan to agreeing to sit on a company's board of directors. In many cases fund managers help set up accounting and cash management systems, make financial projections, recruit executives, make contacts with customers and suppliers and identify additional sources of financing.

There is no question that the SBA's Small Business Investment Companies and Small Business Development Centers are extremely successful and effective at what they do. SBDCs provide valuable information and management assistance to small business owners, but they have, by design, a limited amount of time they can spend with each business owner. SBICs provide critical equity capital to thousands of small businesses across the country, but they tend to focus on larger investments in more investment-ready companies than CDVCs.

Q: What is "capacity building" and why is it necessary?

A: By capacity building, we mean developing an infrastructure that will support and nurture the continued growth of this promising field. So far, the 40 community development venture capital funds at work throughout the nation are showing very impressive results, but the field is still very new. In order for it to grow and fulfill its potential, there need to be more opportunities for training professionals in this highly specialized model, attracting experienced professionals to the field, sharing knowledge and promoting best practices among the different funds, providing technical assistance to the funds themselves, and generating interest in this powerful tool.

Together, these funds are experimenting with and building a model that is different from traditional community economic development, and is not quite traditional venture capital either. It is a new hybrid that borrows sophisticated tools of finance and applies them in promising new ways to some of the most serious and intractable problems of our time. It's a new approach that deserves our attention and our support. The Community Development Venture Capital Assistance Act of 1999 could be the catalyst that enables this field to show its promise. Ultimately, it will be the communities served by CDVCs that have the most to gain.

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COMMUNITY DEVELOPMENT VENTURE CAPITAL:
An Introduction to the Field

The community development venture capital field is a relatively new one. The oldest fund was created in 1966, and most current funds were founded in the last 10 years. Community development venture capital funds (CDVCs) apply the tools of venture capital to fuel business creation and expansion, create good jobs and improve the lives of people in economically distressed communities. CDVCs include nonprofits, for-profits and quasi-public organizations. Their structures range from corporations to limited partnerships, community development corporations (CDCs), limited liability corporations and Small Business Investment Companies (SBICs). Investors in CDVC funds include foundations, banks, insurance companies and other corporations, government agencies and private individuals. They invest because of an interest in the social and financial returns of the funds -- the double bottom line.

CDVC vs. Traditional Venture Capital

Differences Point to Challenges

- Types of Investments
CDVC funds make equity and equity-like investments in highly competitive small businesses that hold the promise of rapid growth. These fast growing companies produce a "double bottom line" of both financial returns and social benefits in the form of good jobs and healthier communities.

-Typical Investment Size
CDVC investments range from $50,000 to $1 million per company, while traditional venture capital investments are rarely less than $500,000 and the majority of such investments are more than $5 million. CDVCs' developmental mission compels them to address the need for smaller investments, which are more expensive to administer and thus less attractive to traditional venture capital sources.

- Operational Costs
CDVCs have higher operational costs than traditional venture capital funds because of the smaller sizes of their deals and the need to provide extensive technical assistance to their investees. Smaller deals require as much staff time as larger ones, forcing CDVCs to spend more time overseeing each investment than a comparably sized traditional venture capital fund. The level of technical assistance that CDVC portfolio companies require further exacerbates this need for additional staff. While traditional venture capital funds' overhead rarely exceeds 2.5 percent of assets, CDVCs' overhead can be as high as 8 or 9 percent.

- Raising Capital
The pool of potential investors that share an interest in the social component of the "double bottom line" is limited, therefore most CDVC funds cannot raise the kinds of funds that a traditional venture capital firm can raise. Existing CDVC funds range from $1.5 to $68 million in size, with most falling between $5 and $10 million. Traditional venture capital funds are rarely

smaller than $25 million, and funds with assets in the hundreds of millions are not unusual. For the CDVC industry to reach an economic scale and demonstrate the full power of the model, substantial new sources of risk capital must be found.

- Technical Assistance

CDVC funds do much more than provide technical assistance; as serious investors with an interest in the success of their portfolio companies, they actually become working partners with entrepreneurs. In many cases, representatives of the CDVC fund will sit on the board of directors, provide day-to-day managerial assistance, help identify additional financing, make contacts with customers and suppliers and help with executive recruitment. They become experts in the industries in which they invest and work alongside business owners to ensure the success of their companies. For businesses in low-income areas, this assistance is often as crucial as the financing itself. As critical as this technical assistance is to the success of the investment, it also adds substantially to the cost of operating a CDVC.

- Deal Flow

Because of their focus on impoverished rural and urban regions, CDVCs generally have significantly fewer deals to choose from. A traditional venture capital fund will review hundreds of business plans in order to select 2 or 3 that it feels are worth investing in. A typical CDVC will evaluate from 5 to 100 deals a year and make 1 to 4 investments. Because the readiness of those deals for investment is usually lower than that seen by traditional venture capital funds, CDVCs also need to provide substantial technical assistance to the companies in which they invest.

- Rates of Return

CDVCs' rates of return are ordinarily less than traditional funds because they are not yet able to reach the same economies of scale as traditional venture capital funds.

# # #

<u>Sources:</u>

Unpublished research by Julia S. Rubin, doctoral candidate in Harvard University's Organizational Behavior Program.

"Community Development Venture Capital," Julia S. Rubin and Kerwin Tesdell, *Community Investments*, Federal Reserve Bank of San Francisco, Fall 1998

COMMUNITY
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VENTURE
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Community Development Venture Capital Alliance

The Community Development Venture Capital Alliance (CDVCA) promotes use of the tools of venture capital to create jobs, entrepreneurial capacity and wealth to advance the livelihoods of low-income people and the economies of distressed communities.

CDVCA has over sixty members, including approximately forty community development venture capital funds. CDVCA's membership is made up of organizations from throughout the United States and throughout the world who seek to apply the powerful engine of growth that has driven the economic expansion in Silicon Valley and other hotbeds of business development to the economic needs of low-income communities. We believe that the combination of equity capital and related entrepreneurial and managerial assistance that community development venture capital funds can provide is a critical part of promoting the growth of local businesses and good jobs in distressed communities.

Community development venture capital is a new field that presents real opportunities to make enduring changes in the lives of low-income people. While the model is promising, there is still much to explore and learn. CDVCA plays a crucial role in fostering this rapidly growing field by:

* providing training and specialized technical assistance
* increasing access to capital and other resources
* collecting and distributing information
* developing standards and best practices
* offering opportunities for peer exchange and learning among professionals
* advocating for the field

* encouraging traditional venture capitalists and individual angel capitalists to become more involved in community development finance.

History

The Community Development Venture Capital Alliance began in July of 1992, when representatives of several community development venture capital funds met to discuss issues of common concern and share experiences and solutions to common problems. They discovered that they had been "reinventing the wheel" in different corners of the country and expressed a desire to establish a regular forum in which they could exchange ideas. Since that first meeting, CDVCA has grown rapidly in membership and activities, bringing together the most experienced practitioners in the field and providing opportunities to learn, explore best practices, and gain resources for their work.

CDVC Profiles:

Examples of Community Development Venture Capital Funds at Work Today

- **Kentucky Highlands Investment Corporation,** London, Kentucky
- **Community Development Ventures, Inc.,** Baltimore, Maryland
- **Coastal Ventures Limited Partnership,** Portland, Maine
- **Boston Community Venture Fund,** Jamaica Plain, Massachusetts
- **Northeast Ventures,** Duluth, Minnesota
- **New York Community Investment Company,** New York, NY

Kentucky Highlands Investment Corporation

P.O. Box 1738
London, KY 40743-1738
Phone: 606-864-5175
L. Ray Moncrief, Executive Vice President and Chief Operating Officer

***

Total Assets: $31 million

Investment Size: $100,000 to more than $1 million

# of Businesses in Portfolio: 8

Legal Structure: Nonprofit 501 (C) (4) Community Development Corporation with several for-profit subsidiaries.

Geographic Focus: Nine counties of southeast Kentucky in Appalachia

***

Founded in 1968 as a Community Development Corporation, **Kentucky Highlands Investment Corporation** invests in start-up and expanding non-retail business enterprises located or willing to move to a nine-county area of southeast Kentucky. With a multi-million dollar capital pool and a portfolio of investments ranging from $100,000 to more than $1 million, KHIC is one of the most substantial funds of its kind in the nation.

The counties that comprise Kentucky Highlands' service area are among the poorest in Appalachia, with income and education levels significantly below the national averages. KHIC provides a multitude of services to businesses in it region, including subordinated debt, equity, real estate construction and management and management consulting services. KHIC carries out its services through the parent organization, and a number of wholly-owned for-profit and nonprofit subsidiaries. KHIC makes equity investments from Mountain Ventures, a for-profit subsidiary, and the parent nonprofit organization. Kentucky Highlands invests in businesses that are located in its target area -- or willing to move there. In many cases, KHIC is responsible for creating new businesses from the ground up. KHIC leadership will identify a market need, write a business plan, finance the plan and then recruit a CEO to run the business.

In 1994, KHIC was designated the Lead Entity for a Rural Empowerment Zone for an area covering three of its counties. As the Lead Entity, KHIC directs the use of $40 million in Empowerment Zone funding and is responsible for the administration and implementation of a strategic plan for the region.

KHIC Portfolio Company:

American Health Management
Kelly Upchurch, President
Richmond, KY

At the age of 32, Kelly Upchurch had an ambitious vision: to open a network of adult day care centers that would offer supervised daytime care for the elderly throughout rural Kentucky. Nationally, there are more than 6,000 such centers -- usually in metropolitan areas -- but Mr. Upchurch believed that rural Kentucky had a tremendous need. So in 1997, he quit his job at a local hospital to start ***American Health Management, Inc.***

A psychologist, with extensive experience in the field of rehabilitation, Mr. Upchurch believed that he had the knowledge and the commitment it would take to run American Health Management. What he needed was financing to get started and business expertise to ensure lasting success. Mr. Upchurch found the exact combination of capital and expertise he needed at ***Kentucky Highlands Investment***

***Corporation (KHIC)**. Ray Moncrief, Executive Vice President and Chief Operating Officer at KHIC (and a CDVCA board member), was impressed with Mr. Upchurch's vision. "I thought his idea was a natural fit for us because it would create professional jobs in a rural area where we need more professional jobs."*

KHIC provided American Health Management, Inc. with a $75,000 equity investment and $15,000 in working capital for its first center, The Clinton Adult Day Health Care, which opened in January 1998 in Kelly's hometown of Albany. As part of the deal, KHIC owns a percentage of the company, which Upchurch can buy back incrementally over a five-year period. The KHIC team also provided countless hours of technical assistance, helping Mr. Upchurch develop his business plan, set up an accounting and cash management system, establish a schedule of regular board meetings, make financial projections, and plan for the future growth of the business. According to Mr. Upchurch, technical assistance was the real appeal of Kentucky Highlands. "They do this every day," says Mr. Upchurch. "I'm strong in health care systems, but they were strong in things I didn't have experience in. Basically, they assigned me a team and gave me the name of a person I could call anytime to ask for advice."

After just over a year in operation, the center -- the first of its kind in the area -- is already making a modest profit. In fact, American Health Management was able to use revenues from that center to finance the opening of its second center in Monticello, Kentucky in 1999. Ultimately, Upchurch plans to open 16 centers and grow American Health Management into Kentucky's largest adult health care center. Mr. Upchurch expects that each center will result in the creation of 6 to 8 quality jobs -- recreational therapists, nurses aids, registered nurses -- in towns where good jobs are scarce.

All staff are hired from within each community and receive competitive wages and health insurance. But Upchurch is just as proud of the fact that these centers enable their patients' caregivers to remain employed. "I think it's a tragedy that someone has to leave the workforce simply because they are taking responsibility for a family member," says Upchurch. "We give people the opportunity to take good jobs and go to work each day with peace of mind."

Community Development Ventures, Inc.

MMG Ventures, L.P.
826 East Baltimore Street
Baltimore, MD 21202
(410) 333-2550
Anthony Williams, Executive Director

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Total Assets: $8 million

Investment/ Loan Size: $100,000 to $500,000 for a term up to 10 years.

# of Businesses in Portfolio: 3

Legal Structure: non-profit 501 (C) (3)

Geographic Focus: Makes investments in businesses located in and around Baltimore's Empowerment Zone and Enterprise Zones.

* * *

Established in 1998, **Community Development Ventures, Inc. (CDV)**, is a non-profit 501 (C) (3) company that utilizes socioeconomic investing as a means to improve the well-being of economically or socially disadvantaged individuals and businesses. Its mission is to strengthen the economic base of distressed communities through business and entrepreneur development. CDV is managed by the **MSBDFA Management Group (MMG)**, a professional asset manager for economic development and private equity funds, including the Maryland Small Business Development Financing Authority and MMG Ventures, L.P, a licensed Specialized Small Business Investment Company (SSBIC)

CDV was developed by MMG to carry out the Baltimore Emerging Business Initiative (BEBI), which seeks to fuel economic development through a combination of venture capital, management and technical assistance, training and entrepreneurial development.

CDV provides senior and subordinated debt and equity to businesses located in and around Baltimore's Empowerment and Enterprise Zones that are in need of growth or start-up capital. In addition to its financing component, CDV offers a Management & Technical Assistance Program (M&TAP) to Baltimore businesses and a Youth Entrepreneurial Program that promotes entrepreneurial awareness and skills among high school students.

To date, CDV has raised a total of $8 million -- $5.7 million in the form of debt and $1.1 million in the form of grant/equity from a variety of sources, including The Ford Foundation ($1.65 million), Prudential Insurance Company ($4.3 million) and Empower Baltimore Management Corporation ($817,500). CDV has also received $1.25 million from the U.S. Department of Treasury's Community Development Financial Institution (CDFI) Fund.

CDV Portfolio Company:

Ntegrity Telecontent Services, Inc.
Dwayne Goldsmith , CEO
Baltimore, Maryland

In 1997, Dwayne Goldsmith and Theresa Osborne, quit their executive jobs at Chicago's Ameritech Corporation to launch ***Ntegrity Telecontent Services, Inc.****, a telecommunications company that provides local and long-distance phone service to small business and residential customers.*

Capitalizing on a spate of deregulation in the telecommunications industry, Ntegrity was established as a Competitive Local Exchange Carrier -- or reseller -- of local and long-distance phone service, enabling it to provide bundled communication services, including paging, voice messaging and Internet service, to its customers.

With a customer base in New Jersey, Pennsylvania and Maryland and the right to resell phone service in Massachusetts and New York, this minority-owned start-up could have been headquartered in any number of northeast cities. But the group decided to move to Maryland after CDV offered it $500,000 in subordinated debt, providing a significant portion of the total $2 million the company needed to meet its working capital, equipment and office development needs.

While Ntegrity did attract the attention of a number of traditional venture capitalists, Ntegrity executives pursued the CDV offer largely because of the consultative services and management assistance that came with it -- something Ntegrity executives believed gave the firm a strategic advantage to other sources of funds.[1] *CDV staff helped Ntegrity (need details on technical assistance).*

In the summer of 1998, Ntegrity Telecontent Services, Inc., moved its offices to its new offices in Baltimore's empowerment zone, bringing 41 job opportunities to the area. As part of its agreement with CDV, it has agreed to fill a portion of these jobs with Empowerment Zone residents. Four neighborhood residents have already been hired. Ntegrity's first year revenues are expected to reach $4.5 million.

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[1] Source *The Daily Record,* Saturday, January 30, 1999, quote from Keith Machen, Ntegrity vice president.

Coastal Ventures Limited Partnership

Suite 302
2 Portland Fish Pier
Portland, ME 04101
(207) 772-5356
Nathaniel V. Henshaw, President

* * *

Total Assets: $5.5 million

Current Equity Investments: $1.9 million

Investment Size: The fund seeks to make equity investments of between $50,000-$500,000 in growing Maine companies.

# of Businesses in Portfolio: 10

Legal Structure: For-profit limited partnership. Subsidiary of a non-profit 501 (C) (3)

Geographic Focus: State of Maine. Can invest small portion of assets outside the state.

* * *

In 1996, **Coastal Enterprises, Inc. (CEI)**, a non-profit community development corporation with a 30-year track record of providing financial and technical assistance to small businesses and housing and social service providers in Maine, established **Coastal Ventures Limited Partnership (CVLP)**, a for-profit limited partnership, to raise, manage and invest socially responsible venture capital funds. CVLP was capitalized at $5.5 million by investments from more than 20 institutional investors, including eight Maine banks, several national foundations and CEI, which serves as a general partner.

CVLP makes equity investments of up to $500,000 in growing Maine companies that can generate above-average equity returns over a five to seven-years,while creating quality jobs and meeting other social goals. In addition to the investment of capital, CVLP provides management assistance and strategic planning, financing and introductions to service providers in the local and national business communities.

Among the most socially oriented of all the CDVC funds, CVLP requires businesses that it invests in to sign an Employment Training Agreement (ETAG), committing the company to train and hire low-income individuals as a result of the growth the fund is financing. Companies are also expected to offer a living wage and some level of health care coverage to their employees. All portfolio companies are screened for positive environmental impacts and progressive management practices. CVLP also gives preference to businesses owned by women or minorities, as well as those located in the poorest sections of Maine. This emphasis on social goals is an outgrowth of CEI's mission which directs economic and human resources to help Maine people and communities, particularly those with low incomes, reach an adequate and equitable standard of living, working and learning.

CVLP Portfolio Company:

Cuddledown of Maine
Christopher Bradley, President
Portland, Maine

***Cuddledown of Maine** was founded in 1973 by Ellen Manson. Manson frequently traveled to Europe, where she discovered fine down-filled comforters and high-quality bedding products. She brought samples back to Maine and friends began asking Manson to bring some back for them as well. Recognizing a good business opportunity, Manson placed ads in U.S. magazines and began selling products by mail order.*

By 1985, Cuddledown sales had grown to $1.2 million, exceeding Manson's comfort level and leading her to sell the business. However, the new owner lacked the necessary dedication *and experience, and sales declined. In August 1988, a family investor group headed by Christopher Bradley purchased Cuddledown and began turning the company around.*

As a growing business, Cuddledown needed capital. However, the company's existing debt level meant that they couldn't approach traditional sources of financing. That's when Bradley turned to **Coastal Enterprises**. *He had heard about CEI's commitment to growing Maine businesses through debt and equity investments.*

CEI worked to secure a $1.2 million financing for Cuddledown, in coordination with the Atlantic Bank, the Small Business Administration, and the Finance Authority of Maine. By 1998, Cuddledown needed additional capital and Coastal Ventures, a community development venture capital fund, came through with a $300,000 equity investment. In addition, CEI assisted in hiring a chief financial officer for Cuddledown by doing the initial screening and supplying a list of the most promising candidates.

Currently, Cuddledown is growing at more than 25% a year. It employs 83 people, and expects to add many more positions in the next few years. All employees receive a benefits package, including a health insurance plan. Wages and working conditions are also excellent and there is very little turnover.

Boston Community Venture Fund

30 Germania Street
Jamaica Plain, MA 02130
(617) 522-6768
Elyse Cherry, President

* * *

Total Assets: $5.5 million

# of Businesses in Portfolio:

Legal Structure: For-profit limited liability corporation.

Geographic Focus: Primary focus is state of Massachusetts. Can invest outside the state.

* * *

The **Boston Community Venture Fund (BCVF)** is a community-based venture capital fund established in 1996 by **Boston Community Capital** (formerly Boston Community Loan Fund), a twelve-year-old $12 million Community Development Loan Fund. BCVF's mission is to invest equity capital in high-potential, emerging businesses in low-income communities in metropolitan Boston and eastern Massachusetts. The BCVF portfolio attempts to reflect a balance of seed stage and growth stage companies, or seed stage companies with substantial value added.

BCVF's primary social objective is to provide stable employment with livable wages; the possibility of upward mobility; and access to training for people living in low-income communities who are at risk of long-term dependence on public assistance but are motivated to improve their economic situation. Portfolio companies must also have a clear means of returning the fund's invested capital with a reasonable profit. These companies require strong management; a growth-oriented business strategy; a target hurdle rate of 20 percent; and anticipated return of investment in five to seven years.

BCVF is currently capitalized at $5.5 million. The fund anticipates increasing that capitalization to over $8 million by the end of 2001. Along with financial returns, BCVF seeks to create respectable employment, deliver needed goods and services, generate positive economic activity, and establish links between lower-income communities and the broader economy.

BCVF Portfolio Company:

SpringBoard Technology
Tony Dolphin, President and CEO
Springfield, Massachusetts

In 1993, Tony Dolphin, an African American entrepreneur, saw an opportunity to create his own business when Digital Equipment Corporation announced that it would close the division in which he was working. Tony had been a General Manager at Digital for more than 10 years and decided to approach the company with a proposal to buy out its hard drive repair division.

*Digital agreed, and Dolphin formed **SpringBoard Technologies,** carving out a niche in the competitive computer repair business, providing computer systems, network products and peripherals to service providers and large computer manufacturers. Despite early successes, Dolphin knew that, to stay competitive, the company would have to be able to respond rapidly to a quickly-changing market. "In this business," says Dolphin, "it's either acquire or be acquired. We need to continually expand our technology capabilities if we are going to stay relevant within this industry."*

*But to make the kind of investment necessary to keep his business competitive, Dolphin had to secure substantial equity capital financing. The company sought and obtained $500,000 from from **Boston Community Ventures.**More* *than 60% of SpringBoard's employees live within a two-mile radius of the company, which is located in Springfield, Massachusetts. SpringBoard is committed to workforce training and development and is working closely with the local community college to create a technical training partnership. This round of community development venture capital financing will create 45 new jobs. "We want to bring people in from the community, give them some basic skills, and help them to advance within the company," says Dolphin. "SpringBoard's inner-city employees have not only the opportunity for good jobs at good pay, but also potential for career advancement."*

"Boston Community Venture Fund is different," observed Dolphin. "They go beyond the money. Once they understood our business, they identified opportunities, directed us to the person to speak with, and facilitated the discussion. That's the value-added piece. That's why their investment is so important to us."

Northeast Ventures

802 Alworth Building
Duluth, MN 55802
(218) 722-9915
Greg Sandbulte, President and Chief Operating Officer

Total Assets: $11 million

Investments to date: $8.3 million

# of Businesses in Portfolio: 23

Jobs created: 695 jobs created or saved since 1989

Legal Structure: For-profit corporation

Geographic Focus: Northeastern Minnesota. Up to 15% of assets can be invested in the rest of the state.

* * *

Northeastern Minnesota is a largely rural area that historically has relied on iron ore production for its economic base. When the domestic steel industry encountered significant foreign competition in the 1980s, and began shutting down obsolete facilities and using cheaper foreign ore, the region was left with few economic opportunities. In 1989, **Northeast Ventures (NEV)** was established as a for-profit community development venture capital fund to help diversify the region's economic base and spur entrepreneurship by making equity investments in local companies.

Northeast Ventures is a for-profit corporation with an unlimited lifetime.In addition to providing capital and technical assistance, Northeast Ventures makes its portfolio companies aware of government placement services that can make it easier for them to hire low-income workers. Northeast Ventures was capitalized by a combination of program-related investments from the Ford and MacArthur foundations; equity investments from the Blandin and Northwest Area foundations, Minnesota Power utility, and Minnesota Technology, a state development organization, and a grant from the Community Development Financial Institutions Fund.

NEV Portfolio Company:

Powerain Systems, Inc.
Stephen Kerr, President and CEO
Tower, Minnesota

In 1990, a group of entrepreneurs approached Northeast Ventures about setting up a car wash equipment manufacturing facility in Tower, a town of 508 people, in one of the poorest parts of Northeastern Minnesota. NEV thought the market opportunity was attractive and that the business could create jobs and bring economic vitality to a region. However, the company had an incomplete business plan and lacked a Chief Operating Officer.

Other assistance was needed before NEV could provide financing for the effort. Northeast worked closely with Powerain's founders to revise the business plan and identify a strong CEO candidate for the company. Northeast also invested $200,000 in equity in the business. Northeast's involvement did not stop after making its first investment.

Over a multi-year period, NEV has talked daily with Powerain CEO regarding subjects as diverse as sales, executive recruitment, strategic planning, distributor relationships, and the financial structure of debt deals. NEV has even worked to locate suitable housing for senior management of the company. NEV has also assisted Powerain in all subsequent rounds of financing, totaling $826,932.

Powerain had a record sales year in 1998 and is expecting another record year in 1999. The company currently employs 20 full-time people, and expects to grow that number significantly in the future. The company provides ongoing training to its staff and entry level positions begin at $8 an hour, with full *benefits. Most employees earn well in excess of $10 an hour.*

New York Community Investment Company

120 Broadway
36th Floor
New York, NY 10271
(212) 693-0870
Howard Sommer, President

* * *

Total Assets: $10 million

Legal Structure: for-profit limited liability corporation

Geographic Focus: Initial $10 million must be invested in New York City. Subsequent $15 million can be invested anywhere in the state of New York.

* * *

The **New York Community Investment Company (NYCIC)**, a for-profit limited liability corporation, was created in 1996 by a consortium of New York City commercial banks to provide creative financing solutions to New York's small business community -- particularly businesses located in low-and moderate-income neighborhoods and businesses owned by women and members of minority groups.

Member banks set up and capitalized the corporation with $10 million to identify potential new deals for the banks to invest in, but also to help meet their federal Community Reinvestment Act obligations. NYCIC provides equity and subordinated debt to companies with sales from $1 to $10 million, and that are located in the five boroughs of New York City. The fund focuses especially on women- and minority-owned businesses, as well as on businesses located in lower-and middle-income areas of the city, but does not restrict itself to these criteria. Furthermore, by limiting itself to a particular demographic target, the fund would be significantly limiting its deal flow, and its ultimate financial performance. NYCIC also does not utilize any social screens, impose any job creation requirements on its portfolio companies, or exclude any industries from consideration for social reasons.

NYCIC Portfolio Company:

Square One Design
Anne Jaroszewicz, President and CEO

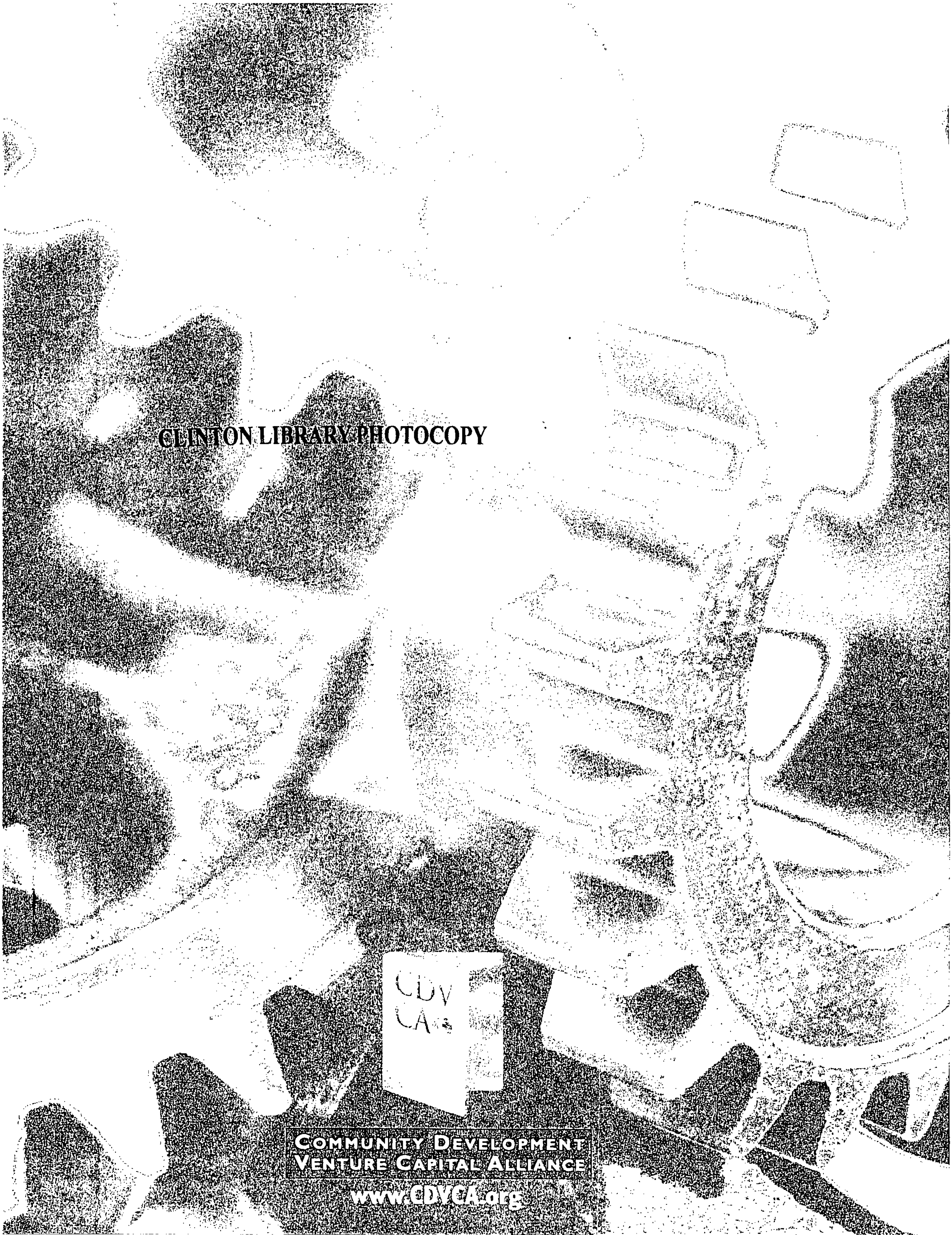
For years, people in the home furnishings industry told Anne Jaroszewicz to come out from behind the curtain of private label design and start her own product line. Her New York City-based company, ***Square One Design,*** *had established a reputation over more than 10 years, developing home furnishing accessories for some of the biggest retailers in the country. But market forces were pushing more and more retailers to bring their work in-house and Square One's business was beginning to flatten.*

Starting her own product line, however, would be tantamount to building a business from the ground up. Ms. Jaroszewicz would need financing for a whole new infrastructure, to warehouse and manage her inventory, establish systems for tracking orders and billing, and hire staff to manage the anticipated growth. And although Square One had an impressive track record -- with customers as notable as Pier 1 Imports and Pottery Barn -- few banks were interested in financing the expansion of a small business. Fortunately, one bank gave Ms. Jaroszewicz a hot tip, suggesting she send her business plan to the ***New York Community Investment Company.***

Ultimately, NYCIC provided Square One with $250,000 in the form of convertible debt that can, at NYCIC's option, be converted to shares of the company. As a direct result of this financing, Chase Manhattan Bank loaned Square One an additional $325,000. With this *new infusion of cash, Ms. Jaroszewicz launched her own line, **Annie J.***

According to NYCIC president Howard Sommer, Ms. Jaroszewicz was a "good example of a company that might not have been able to grow without this new capital." In addition to financing, NYCIC also lent Square One the time and expertise of one of its summer interns -- a business graduate student -- to help the company develop a plan for upgrading the company's accounting and management information systems.
To ensure that the company can keep up with the growing demand for its product, Square One has created several new jobs at a range of skill requirements, from warehouse jobs -- paying nearly double the minimum wage with benefits -- to a national sales manager position. The company rented 7,000 square feet of warehouse space in Red Hook, Brooklyn, hired a manager and two full-time staff to staff it, and is currently recruiting additional warehouse workers and an on-site customer service representative. In the Manhattan showroom, Square One will also add a number of support and professional staff positions.

"NYCIC's money came into the business at the right moment, allowing us to fuel this growth," said Jaroszewicz. "Right now, we are more than 24 percent ahead of our most optimistic projections and if we are able to stay on this trajectory, we will more than double the business we did last year."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