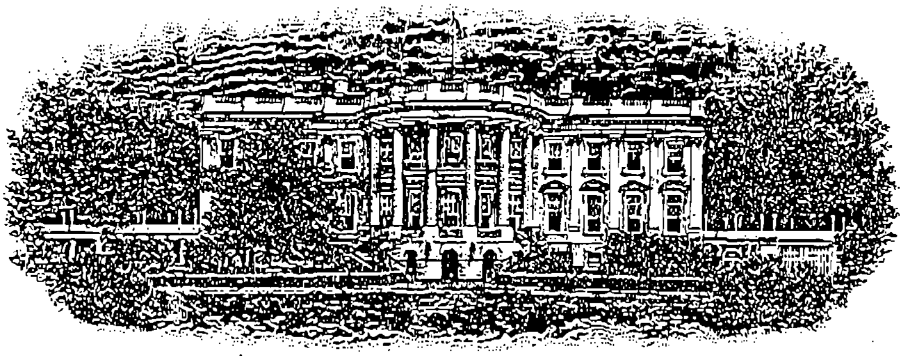

ARC

THE WHITE HOUSE

SARAH ROSEN
SENIOR POLICY ADVISOR
NATIONAL ECONOMIC COUNCIL
202-456-2223 (fax)

TO: Lisa Green

PHONE:

FAX: 752-4231

DATE: 4/7/99 PAGES TO FOLLOW: 30

COMMENTS:

If this fax is incomplete or you need to give clearance information for a meeting, please call Sonyia Matthews at 456-5351 or e-mail "Matthews_S@opd.eop.gov". Thank you.

APPALACHIAN REGIONAL COMMISSION
A Proud Past, A New Vision

ARC

TENTATIVE AGENDA

WHITE HOUSE BRIEFING ON NEW MARKETS INITIATIVE

April 9, 1999

10:15 am – 10:30 am	Welcome and Introductions:
	• Gene Sperling, Assistant to the President and Director, National Economic Council • Jesse L. White, Jr., ARC Federal Co-Chairman • West Virginia Gov. Cecil Underwood, ARC State's Co-Chairman • Gov Patton
10:30 am – 11:00 am	White House Overview of New Markets Initiative:
	• National Economic Council - • Small Business Administration - • Housing and Urban Development • Treasury -
11:00 am – 11:20 am	State Responses:
	• North Carolina • Pennsylvania
11:20 am – 12:30 pm	Discussion and Q/A
12:30 pm	Adjourn

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White House Briefing
Equity Capital for Rural Communities
April 9, 1999

Thursday, April 8, 1999

Overnight at
The Hotel Washington (202) 638-5900
15th & Pennsylvania Avenue, NW,
Overlooking the White House

[Sleeping rooms are reserved in your names at the Government rate of $131.68 tax inclusive. If you need reservation assistance, please contact Anne Bethea at ARC (202) 884-7703.]

Friday, April 9, 1999

[The day's events are being held within a two-block area of the hotel. Please wear comfortable shoes to accommodate short strolls between the events.]

8:00 a.m. — 9:30 a.m.

Orientation Breakfast
The Hotel Washington
Sky Room – Roof Top

10:15 — 12:30 p.m.

White House Briefing
Old Executive Office Building
Treaty Room

[Please bring a picture I.D. for White House entry.]

12:45 — 2:00 p.m.

Lunch Debriefing
Old Ebitt Grill
Cabinet Room
675 15th Street, NW

[Since the day's schedule ends after the hotel's 1:00 p.m. checkout, you may want to check out in the morning before departure for The White House. The hotel will be happy to provide storage for your luggage.]

APPALACHIAN REGIONAL COMMISSION
A Proud Past, A New Vision

ARC

ARC'S CHALLENGING TASK

Congress established the Appalachian Regional Commission in 1965 to bring more than 400 counties in the 13-state Appalachian Region into the mainstream of the American economy, to make these 21 million people and their hundreds of communities contributors to, rather than drains on, the national resources. ARC seeks to equip Appalachian citizens and communities with the entrepreneurial skills, enterprise development resources, and basic infrastructure they need to create self-sustaining local economies.

FLEXIBLE PROGRAMS

ARC's programs fall into two broad categories:

- **a 3025-mile corridor highway system** to break the regional isolation created by mountainous terrain and thereby link Appalachian communities to national and international markets. Roughly 79% of the Appalachian Development Highway System is either completed or under construction.

- **an area development program to create a basis for sustained local economic growth.** Ranging from water and sewer infrastructure to worker training to business financing and community leadership development, these projects provide Appalachian communities with the critical building blocks for future growth and development. This sweeping range of options allows governors and local officials to tailor the federal assistance to their individual needs.

A UNIQUE PARTNERSHIP

The Appalachian Regional Commission represents a unique partnership between the federal government and the 13 states we serve. The Federal Co-Chairman of ARC–appointed by the President and confirmed by the Senate–has one half of the votes on the Commission and the 13 governors have the other half. No policy can be set or any money spent unless the federal representative and a majority of the governors reach agreement. The ARC model represents neither the dictation of policy from Washington nor the abdication of policy to the states; rather, it is true collaboration.

ARC employs a "bottoms up" approach, with projects originating at the local level, primarily through the 71 local development districts (multi-county planning agencies) that ARC supports. As a reflection of this, the governors of all 13 ARC states (nine Republicans and four Democrats) have declared their strong support for the Commission.

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ARC'S STRATEGIC PLAN

Drawing upon advice gleaned from a series of interstate town forums, focus groups across Appalachia, and a regionwide satellite town meeting, the Commission in 1996 unanimously approved a strategic plan that guides ARC's investments in the region. The plan identifies five goals that will enable Appalachian communities to create opportunities for self-sustaining economic development and improved quality of life--**developing a knowledgeable and skilled population, strengthening the region's physical infrastructure, building local and regional capacity, creating a dynamic economic base, and fostering healthy people.**

All ARC projects must be directly linked to at least one of the goals, and project proposals must include plans for measuring performance and gauging the project's success and impact. Typical projects include water and sewer systems for industrial parks or rural households, adult basic skills training and workplace learning, construction of small business incubators, telecommunications strategic planning and implementation, entrepreneurship education, and small business lending.

Projects normally require state or local matching funds and encourage partnerships with the private sector and the non-profit community. ARC grants can also help communities with few resources meet matching requirements for other federal grant programs.

REGIONAL PRIORITIES AND TARGETING OF FUNDS

Believing that Appalachia's future economic vitality depends on nurturing home-grown firms, ARC recently launched a special three-year funding initiative to foster **entrepreneurship** and help the region's communities grow their own businesses. The initiative supports activities in five areas critical to entrepreneurship: access to capital and financial assistance; technical and managerial assistance; technology transfer; entrepreneurial education; and entrepreneurial networks. This emphasis builds upon three earlier special initiatives addressing economic development needs that reach broadly across the region—**telecommunications, internationalization of the economy, and the development of local civic leadership**. After three years of targeted funding, these have now become regular components of the states' plans for using ARC funds.

The Commission allocates a portion of its area development funds for use exclusively in the region's most economically distressed counties. To be classified as distressed, an Appalachian county must satisfy three criteria: per capita market income no greater than two-thirds of the national average, unemployment rate at least 150 percent of the national level, and poverty rate at least 150 percent of the national rate. The Commission reviews the criteria annually and produces a new list of counties each year, based on the most recent data. Currently 108 of the region's 406 counties are classified as distressed.

HOW ARC WORKS

Each fall the Commission distributes its congressional appropriation by formula to its member states. Funds are distributed in three broad categories: highways, area development, and local development district support. Following the distribution of funds, the Appalachian governors, in consultation with the local development districts, prepare strategy statements, linking state priorities and projects to the five goals in ARC's strategic plan.

The Commission staff of about 60 people, most of whom serve as program and financial analysts and researchers, work closely with the State Alternates and Program Managers who oversee the states' ARC program and serve as the state-level contact for those seeking ARC assistance. The process is completed when the Federal Co-Chairman reviews a project and approves it.

A RECORD OF ACCOMPLISHMENT

ARC's programs have produced improved standards of living and greater economic opportunities for the people of Appalachia.

- The regional poverty rate has been cut in half, from 31.1% in 1960 to 15.2% in 1990; the percentage of adults with a high school education has doubled (from 32% in 1960 to 68% in 1990); and the region's infant mortality rate has been cut by two-thirds.

- More than 700,000 Appalachians now have access to clean water and sanitation facilities through ARC projects.

- A network of more than 400 primary health care clinics and hospitals has been completed with ARC funding and now serves 4 million Appalachians a year.

- Since 1977, grants to revolving loan funds–currently $28.4 million–have assisted 1,105 small businesses in creating 21,876 new jobs and saving 24,140 existing jobs.

- A 1993 National Science Foundation-funded study compared ARC's 399 counties with statistical "twin" counties and found that personal income and earnings had grown 48 percent faster in the ARC counties than in their twins.

- In 1998 alone, ARC grants helped provide water and sewer service for 41,468 households, assisted in the development/retention of 35,194 jobs, provided training and educational activities for more than 50,000 Appalachian residents, and placed 192 doctors and dentists in medically underserved areas of the region.

THE JOB IS NOT YET COMPLETE

Despite these successes, many portions of Appalachia still do not participate fully in the strength of the American economy. Additional assistance is needed to overcome a century of neglect.

- In 1996 Appalachia's per capita income was only 83% ($20,179) of the U.S. average ($24,436), and the poverty rate for the region is 14% higher than the national average.

- 108 Appalachian counties are severely distressed, suffering from above-average rates of unemployment, poverty rates that are at least 150% of the national average, and per capita incomes that are less than two-thirds of the national average.

- Key segments of the Appalachian corridor highway system are not yet under contract.

- Even with ARC funding, Appalachia receives 13% less in direct per capita federal spending than the national average.

FUNDING LEVEL

Last year Congress and the President approved a three-year reauthorization for ARC's area development work, with authorization levels of $67 million in FY 1999, $68 million in FY 2000, and $70 million in FY 2001. The actual area development appropriation for FY 1999 is $66.4 million. For the first time Congress also authorized funding of the Appalachian Development Highway System out of the Highway Trust Fund. TEA-21 authorizes $450 million a year for work on the ADHS. The total authorization for all ARC programs for FY1999 is $517 million.

The President's budget for FY 2000 calls for $66.4 million for the Commission's area development activities and an obligational ceiling of $405 million for the highway system.

For more information on the Appalachian Regional Commission, please visit ARC's website at **www.arc.gov**.

February 1999

APPALACHIAN REGIONAL COMMISSION
A Proud Past, A New Vision

Building Entrepreneurial Economies in Appalachia

The Appalachian Regional Commission

The ARC Regional Initiative in Entrepreneurship

The Commission has launched a 3 year, $15 million regional initiative in building entrepreneurial economies in Appalachia. The ARC views entrepreneurship as a critical element in the establishment of self-sustaining communities that create jobs, build local wealth, and contribute broadly to economic and community development. ARC's goal is to promote locally-owned, high value-added, sustainable ventures that increase local wealth inside Appalachia, foster human and social capital and reduce the need for outside government and philanthropic subsidies.

Background: The Changing Economy

Entrepreneurship and small businesses are playing a major role in the restructuring of the U.S. economy and in creating jobs. On the eve of the 21st Century, the barriers to world commerce have declined as information has become more accessible, competition has intensified and markets have become more international. As a result, large firms are downsizing, reorganizing and relocating, often overseas, to remain competitive. In this era of flexible specialization, many small firms are capitalizing on their ability to adapt to meet rapidly changing market demands. But states and communities that do not find ways to capitalize on the strengths of small and medium-sized businesses to diversify their economies risk marginalizing their future development potential. The challenge for states and communities throughout Appalachia, as well as the rural United States, is how to foster the economic and cultural conditions that give birth to entrepreneurs, support innovation, and assist in the development and expansion of successful enterprises.

Appalachia's future economic vitality, in large measure, depends on nurturing home-grown firms, encouraging innovation and risk-taking and enhancing investment in new businesses. Appalachia needs to cultivate resourceful entrepreneurs who not only create value by recognizing and meeting new market opportunities, but who increase the value-added within the region. While the region has several outstanding examples of entrepreneurial communities and organizations, and possesses many entrepreneurial assets, including the self-reliance of its people, it also faces many challenges. These entrepreneurial shortcomings stem from the region's longstanding dependence on extractive industries and branch plant manufacturing, and the presence of many absentee landlords who have siphoned off value from the region. Furthermore, the culture of entrepreneurship is neither broad nor deep throughout the region, and anecdotal evidence and preliminary research findings suggest that there are many gaps in the infrastructure for supporting entrepreneurship, ranging from technical assistance to development finance.

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Building an Entrepreneurial Economy in Appalachia: ARC's Strategy

ARC subscribes to the view that entrepreneurial activity can be nurtured through a variety of educational, business assistance and capacity building initiatives. After a year long development process involving region-specific research, local focus groups and consultations with regional and national experts, the ARC adopted a strategy designed to strengthen those key factors that play a central role in stimulating and sustaining entrepreneurship. Together these factors make up the infrastructure that supports entrepreneurial economies and they include:

- **Access to Capital and Financial Assistance** - Finding the initial start-up capital for a new business is often the most daunting hurdle for an entrepreneur to clear, particularly equity capitalization, but other hurdles rapidly confront the new business, including finding adequate working capital and credit for building up inventories. Other financing problems include finding seed capital for new technological innovation, loan packaging assistance and long-term debt financing for newer companies or businesses that are seeking to expand. A wide range of private and public institutions play a role in servicing these financial needs, but the role of development finance institutions is particularly important for rural regions like Appalachia, as these organizations often provide both finance and technical assistance to new and expanding small businesses.

- **Technical and Managerial Assistance** - While capitalizing businesses is important, for a majority of entrepreneurs, the key to launching a business, as well as surviving and thriving past the first year is acquisition of or access to sufficient technical, managerial, and financial expertise. Such business management expertise is essential for enterprise development, from early stage activities, including market feasibility studies, business planning, financial planning and packaging, to on-going marketing, accounting, procurement advice, export assistance and management and legal capability. Such services, as well as other more specialized assistance, are available from a wide range of private and public sector providers, including business consultants, business incubators, colleges and universities, financial institutions, small business development centers and economic development agencies. However, anecdotal evidence suggests that the availability of these services range from fragmented at best to nearly unavailable.

- **Technology Assistance** - Technological innovation by new and existing businesses often lies at the heart of enterprise development and brings with it a host of problems that may confound success unless they can be solved in an efficient and timely manner. The technological assistance required by businesses includes a wide range of services, such as engineering services for product development and manufacturing process design, technology transfer programs to promote commercialization of technologies from universities, public laboratories or large firms, innovation seed grants, research and development financing, patent and licensing assistance and technology-based incubators;

- **Entrepreneurial Education and Training** - Educational and training institutions play a key role in stimulating entrepreneurship through the introduction of entrepreneurial content into the curriculum of primary and secondary school courses. At the secondary education level, non-profit organizations, as well as business and trade groups, can help start and assist in developing such programs through cooperation with schools and by providing alternative educational venues, including mentoring programs. In addition, conducting hands-on activities that expose students to entrepreneurial environments permit them to explore the tasks and challenges of enterprise development. Post-secondary educational institutions also play an important role as both two and four-year colleges and universities can offer more advanced educational and training courses to provide managerial and technical assistance and information to entrepreneurs and those who wish to start businesses.

- **Entrepreneurial Networks** - Formal and informal networks of professional and trade service providers link firms together to improve customer services, share resources, develop markets and solve problems that are usually beyond the scope of an individual firm. Such service provider networks often knit together various business, technical, educational and training and information services to realize synergies in providing a *one-stop shop* for their customers, even though all the providers are not under one roof. Moreover, collaboration among service providers often generates unique information resources for participants and can stimulate new types of innovations in services and new market opportunities. An entrepreneurial network can coordinate the provision of services to customers and supply specific resources that are unique to the network, such as information services. The types and extent of such entrepreneurial services networks in the Appalachian region are largely informal and need to be documented.

- **Entrepreneurial Community Culture** - Communities can foster the emergence of entrepreneurs by encouraging the values of innovation, creativity, and can-do attitudes among the citizenry and within various institutions. Both civic and business leaders must take an active role, if such an entrepreneurial culture is to develop.

A Regional Initiative

The ARC believes that all of the above elements are essential to building vibrant entrepreneurial economies and that it is possible and desirable to stimulate greater levels of entrepreneurship by deepening and expanding this infrastructure in the Appalachian region. Building local business activity based on local talent and resources will take time and the participation of numerous persons, organizations, and institutions. The ARC is committed to an initiative that will build the capacity of existing institutions and organizations, develop or expand the coordination and networking of services and programs that support entrepreneurial activity, and initiate efforts to fill the gaps in or a person's access to the entrepreneurial infrastructure in our Appalachian communities.

APPALACHIAN REGIONAL COMMISSION
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Regionwide Entrepreneurship Activities

In addition to funding individual entrepreneurship projects in each of the region's 13 states, ARC is implementing a variety of regionwide activities to address identified gaps in, and build the institutional capacity within, the five key elements of an entrepreneurial economy: access to capital and financial assistance; technical and managerial assistance; technology transfer; entrepreneurial education and training; and entrepreneurial networks. One broad focus of all these activities will be to leverage support from other institutions, including support from federal agencies and the foundation community, to expand the effectiveness of this work and build a broader institutional base of support for economic development activities in the region.

ARC staff are currently developing plans to integrate the Administration's New Markets Initiative into these activities, several of which blend well with the NMI proposals.

Capital Access. Existing research on capital gaps in the region, conducted by Mt. Auburn Associates in 1998 under contract to ARC, reveals significant gaps in the availability of equity capital and working capital financing. ARC is working to eliminate these gaps by promoting the development of a seamless capital system. An informal public-private sector advisory group of development finance experts and regional finance professionals has been created to assist ARC in identifying opportunities to best assist the region. Activities to be undertaken include: promotion of equity-oriented strategies and support for the development of equity funds; information sharing and targeted training among community development financial institutions; review of the structure and outcomes of the ARC Revolving Loan Funds; and development and promotion of programs to close the gaps for working capital financing.

ARC is collaborating with the Small Business Administration in helping with the roll-out of its workshops on SBIC investments in rural America and the Inner City. Federal Co-Chairman Jesse White will be a featured speaker at the Atlanta workshop, and ARC will be aggressively promoting the workshop throughout the region.

Entrepreneurial Education & Training. Appalachia is experiencing a rapid proliferation of entrepreneurial training and education programs, with providers ranging from private non-profits, community colleges, local chambers of commerce, and local development districts (multi-county economic planning and development agencies). ARC staff are helping to identify the current needs of entrepreneurial training and education providers and clients in the region, and the need for development of new curriculum or the consolidation of existing curricula/best practices. ARC will also pursue opportunities for sharing information among practitioners through practitioner training(s), the development of peer networks and an information clearinghouse.

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Sector-Based Strategies. By identifying regional strengths and weaknesses, industries which have particular competitive advantages in the target communities can be highlighted and their growth strategically supported. Ensuring private sector participation and leadership (through network development) is a key ingredient to the success of this approach, as is creating partnerships between distressed counties and other counties to focus on overcoming barriers to growth in the targeted sectors. In January ARC sponsored a regionwide forum on the benefits of strategic sectoral approaches to economic development, designed to educate practitioners and foster alliances with private sector service providers. The Commission has just released a Request for Proposals for innovative projects that will strengthen strategically important sectors or clusters in order to support local entrepreneurs.

Incubator Networks. This activity will support new and strengthen existing incubators in the region. Sub-regional networks of incubators will be developed to share experiences, identify best practices, avoid duplication, maximize partnership opportunities and provide technical assistance as needed. An advisory committee of local incubator managers is guiding this work.

Technology Commercialization. Research indicates that the commercialization – and hence economic benefit–of new technologies developed in ARC states typically occurs in more urban communities outside the Appalachian portion of the state. In partnership with universities and private firms in the region, ARC will provide support to efforts targeted at commercializing new technologies within our rural communities. Activities will include support for: regional forums to share learning(s) and best practices among participating institutions; convening of public and private sector partners to build stronger bridges for technology commercialization; and the development of new and innovative rural commercialization strategies.

February 1999

APPALACHIAN REGIONAL COMMISSION
A Proud Past, A New Vision
ARC

Date: March 31, 1999

To: ARC State Alternates and Program Managers

From: Thomas M. Hunter, Executive Director

Subject: Capital Access and Credit Needs in Appalachia

The Appalachian Regional Commission (ARC) believes that small, homegrown businesses play an important role in creating self-sustaining, local economies and in improving the quality of life in Appalachian communities. In 1997, ARC launched a three-year, $15 million Entrepreneurial Initiative to ensure that Appalachian communities have the commitment and resources necessary to assist entrepreneurs in starting and expanding local businesses.

While ARC continues to work on the fundamental building blocks of economic development—highways, education and training, industrial infrastructure, water and sewer, telecommunications, leadership development and health care—creating a homegrown business base requires a different set of resources.

Three factors are essential for an entrepreneurial economy to grow and develop: first, a belief among the people that they can grow their own successful businesses; second, access to equity and debt capital throughout the early cycle of a new business; and third, readily available technical and managerial assistance to small businesses that are starting or expanding. ARC's entrepreneurial initiative is working to address all three of these areas.

Yet, ARC recognizes that the public sector cannot do the job alone; that is why we need the private sector to join our unique federal-state partnership to create alliances and new vehicles to get the needed capital and technical assistance to those areas that need it most. For these reasons ARC welcomes the opportunity to examine new approaches to encourage and attract private capital into the Region.

Overview on Capital and Credit Needs in the Appalachian Region

Capital and credit gaps for rural businesses have been identified as a significant regional problem in research conducted by the Federal Reserve Board, the Appalachian Regional Commission and the Economic Research Service of the U.S. Department of Agriculture.[1]

[1] See *Financing Rural America*, by the Federal Reserve Board of Kansas City, April 1997; *Capital and Credit Needs in the Appalachian Region* by Mt. Auburn Associates, February 1998, Appalachian Regional Commission, Washington D.C.; *Credit In Rural America, 1997* by the Economic Research Service, Rural Economy Division, U.S. Department of Agriculture, Agricultural Economics Report No. 749, April 1997.

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These studies reveal that while the availability of capital for fixed asset financing—such as real estate, plant and equipment—appears to be readily available at competitive rates from private and public financial institutions, significant capital gaps exist in the availability of equity capital for start up firms and for certain types of working capital financing. In addition, the studies find:

- There is a lack of diversity in financial institutions serving rural areas and in Appalachia, and rural businesses are over dependent on commercial banks.

- Financial market conditions are least favorable for businesses in persistent poverty areas because they have fewer banking choices and lower levels of competition.

- The most significant gap for rural businesses is the availability of equity or risk financing, particularly for start up firms and small business expansions in older, more mature industries.

These studies indicate that several factors limit the inflow of investment capital to rural businesses, particularly for equity capital investments:

- A lack of information about viable opportunities in many new and expanding businesses in rural areas due to the remote or isolated character of the Region;

- The lower population density in rural areas makes it more expensive to develop the deal flow of potential equity investments;

- A higher incidence of business deals in mature and traditional businesses with average rates of return and growth rates;

- A greater need for technical assistance in preparing and marketing business plans to investors to improve the flow of bankable deals;

- The smaller average size of deals in rural areas, and the lack of professional services such as accountants, lawyers, consultants, industry associations, and peers increases the costs of putting together such deals.

For these reasons, rates of return do not meet the threshold levels of traditional venture capital firms.

Surveys of both rural businesses and equity investors located within or near rural areas have provided the most reliable information on the demand for equity capital requirements by type and size of businesses. [2]

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[2] See *Capital and Credit Needs in the Appalachian Region* by Mt. Auburn Associates, February 1998, page 61, Table 4.2.

- Within Appalachia, a sample of businesses in both manufacturing and service sectors reveals a greater reliance on personal resources for equity investment, and less access to venture capital investors than their urban counterparts.

- An analysis of business demand for financing from the existing SBICs and venture and development venture capital funds in or near the Appalachian Region, indicates a pattern similar to national trends, with venture equity sources ranking behind personal savings, second mortgages, family and friends, and business colleagues. Even after controlling for differences between metro and non-metro areas, the relative rankings for the importance of venture investment indicates a considerable demand for venture investment.

Research conducted by the Federal Reserve Board on the number and dollar value of initial public offerings, both venture-backed and non-venture, shows that when rural companies go public their terms are competitive with the national market.[3] The Small Business Administration has documented the need for greater access to equity capital investments for smaller sized investments in the $100,000 to $300,000 range.

Existing Capital and Credit Programs in Appalachia

While many of these market obstacles are being addressed by current financial service providers in the Region, a survey of existing equity investors and specialized lenders in the Appalachian Region shows an uneven geographic distribution of various types of providers.

- *Equity funds* located in or near the region are structured to invest in traditional venture capital deals, requiring exit strategies and rates of returns unsuitable for many of the region's businesses. There are 79 funds that operate in or near the Appalachian region, including *Small Business Investment Corporations* and private venture funds, with total assets for those funds that disclose such information of $2 billion. Only 48 of these funds, however, are actually located within the ARC region with assets totaling $375 million. In addition, there are eight statewide state-sponsored equity-type funds.

  Small Business Investment Corporations in Appalachia (See attached map.)

  - Currently there are 13 SBICs licensed within the Appalachian region, but few actively service rural areas;

  - There are particular gaps in coverage for Appalachian Ohio, Mississippi, Maryland, New York, Georgia and Virginia.

[3] See "Developing Rural Equity Capital Markets" by David Brophy, in *Financing Rural America*, by the Federal Reserve Board of Kansas City, April 1997, pp. 159-172.

- To a lesser degree there appears to be sparse coverage in other states such as Kentucky, North Carolina, Tennessee—although the proprietary nature of these funds makes it difficult to ascertain whether SBICs located in nearby cities actually service the Appalachian portions of their respective states.

- Kentucky Highlands Investment Corporation's Mountain Ventures stands out as the one active development venture fund that services the rural Appalachian portion of the state;

- Pennsylvania, West Virginia and Alabama have a few SBICs concentrated in just a few cities to serve each state, but there is little evidence that they service the rural portions of their states;

- North Carolina and South Carolina each recently added SBICs in the Appalachian portions of their states.

Private Venture Investment Companies in Appalachia (See attached map.)

Of the 66 private venture investment companies located in or near the Appalachian Region, only 36 are actually operating within the Appalachia with Pennsylvania and West Virginia accounting for 31 of these funds. Moreover, most of the Pennsylvania are concentrated in Pittsburgh. Of the funds that disclose their assets, only $170 million of the $860 million are held within the Region.

State Venture-Type Funds

Eight of the Appalachian states have publicly backed venture-type funds, with some equity features, but most of these programs have focused on a statewide efforts to recruit or develop high technology businesses. Some have provided financing for business franchises and acquisitions. A few of these programs provide early-stage seed capital, but fewer offer developmental venture capital for distressed areas.

- Existing *Revolving Loan Funds* programs provide debt financing to businesses for deals that are typically well collatoralized and 'bankable.' There are 27 ARC-sponsored RLFs in operation, with ARC's capitalization at $22.8 million. In addition, there are 84 other RLF programs supported by EDA, HUD, Rural Development and the individual states within the Region.

- *Micro-loan funds* and *community development loan funds* provide very small loans, with micro-loans typically providing loans of less than $10,000 and community development funds typically providing loans in the $35,000 to $45,000 range. There are 37 micro-enterprise funds in the region, representing $9.4 million in assets, and 14 community development loan funds, with 5 representing assets of $55 million.

Responses to Capital Gaps

The uneven coverage within the Region underscores the prevalence of market barriers to the provision of capital and credit. Some of these barriers can be addressed by policies that overcome information deficits, provide technical assistance to increase deal flow, spread investor risk through consortiums and guarantees, match private funds with public funds, and thereby attract capital and credit providers to the region.

A menu of options has emerged from separate initiatives including those conducted under the aegis of the Appalachian Regional Commission's Entrepreneurship Program and the Small Business Administration's existing and proposed initiatives. The following attachments briefly describe a range of possible approaches, particularly for addressing the scarcity of equity capital in the Region.

Appalachian Regional Commission's
Innovations in Development Finance Committee
Proposals for Discussion
Developed at January 22, 1999 meeting in Charlotte, NC

Equity Capital

Goal: To improve the flow of non-venture equity capital to Appalachia to provide support for businesses starts and expansions. The objective discussed was the creation of 4 to 7 equity vehicles capitalized at $10M - $20M each.

Issues and Recommendations: To achieve these goals, the committee recommended consideration of a three-faceted approach:

- developing quality fund managers;
- creating new funds or building on existing institutions, and;
- supporting fund capitalization.

I. *Management* – the top priority need is to develop quality fund managers. Committee members believed that capitalizing investment pools once a qualified management team is assembled is not a significant obstacle. Recommendations to improve management capacity in the Region include:

- Bring specialized training programs to the Region.
- Provide internship opportunities for development finance personnel to work in venture capital funds
- Involve traditional venture capitalists on boards of directors of community development venture funds.

II. ***Expand Existing Programs or Create New Entities***

A. Expand Existing Programs

In some cases existing programs (Revolving Loan Funds, micro-credit funds, etc.) could expand their missions and develop equity programs. The committee underscored the importance of ensuring that candidate institutions have the capacity to undertake development venture capital as not all debt fund managers have the requisite skills to invest and manage equity portfolios.

B. Create New Entities

In other cases, new entities would need to be created. Committee members believed that sub-regional funds focusing on one or more states would be more effective than a large 13-state fund. This approach would allow local funds to select the structure (Small Business Investment Companies, community fund, venture fund, etc.) that best suits local needs, and to leverage existing service providers networks to enhance deal flow.

III. ***Capitalization*** – funds could be capitalized from a range of sources including investments from private financial institutions, foundations, and public sources. Recommendations to capitalize funds include:

1. Revise ARC's Revolving Loan Funds (RLFs) guidelines to allow transfers of capital from RLFs into approved community equity funds.

2. Identify regional investment opportunities relating to initiatives by the Federal Home Loan Bank system, and the Small Business Administration (particularly formation of more Small Business Investment Companies).

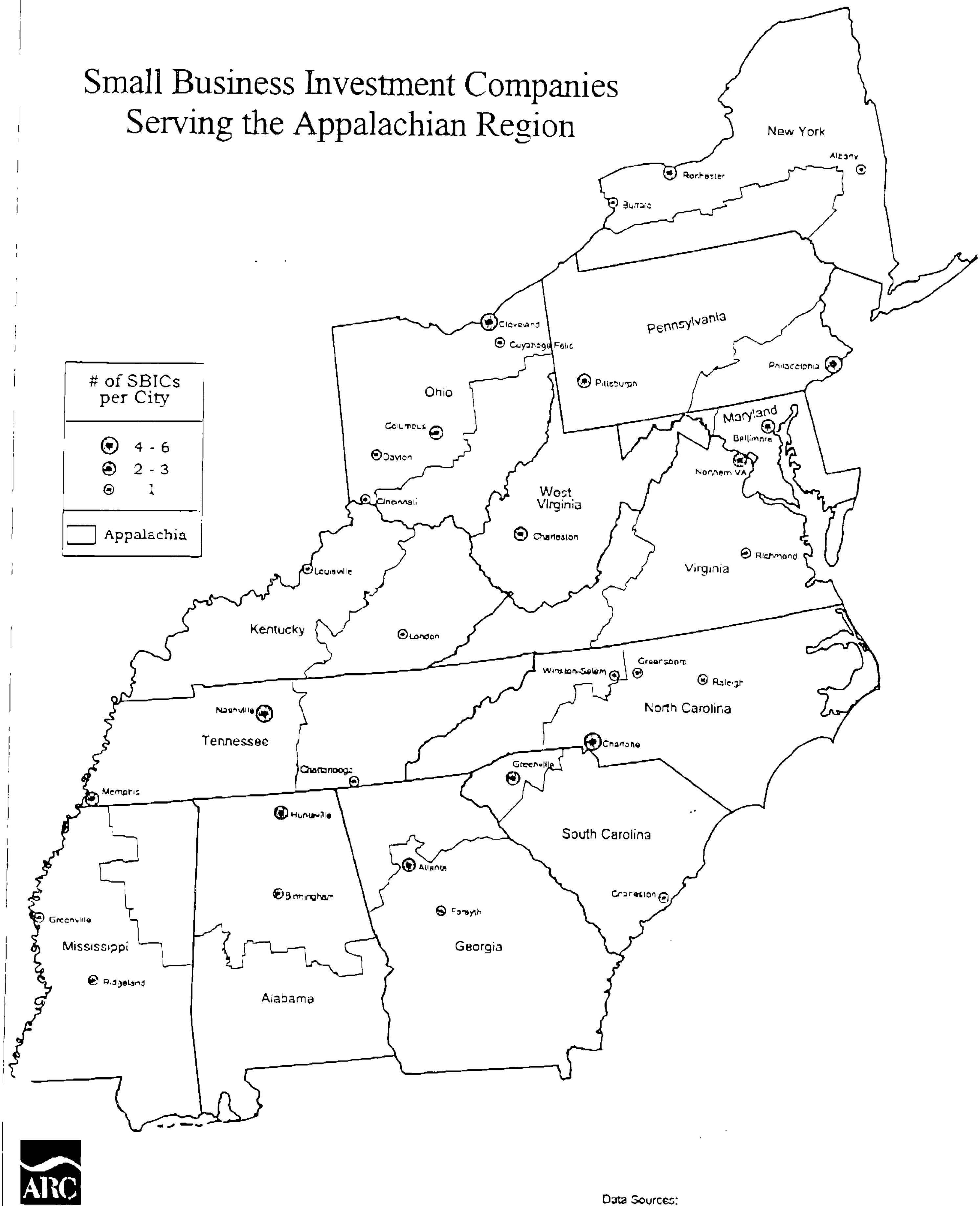
3. Convene a series of sub-regional Rural Equity Summits (2 to 4 venues), co-sponsored with the above partners, to include participation of the hosting Governors and the White House, with interested fund managers invited to attend. The objectives would be:

   - educating private investors about these new community development opportunities (which meet new CRA guidelines);
   - matchmaking public and private investors; and
   - hosting of a high-profile in-Region event focused on solutions.

4. Work with foundations to find investors for capitalizing sub-regional funds.

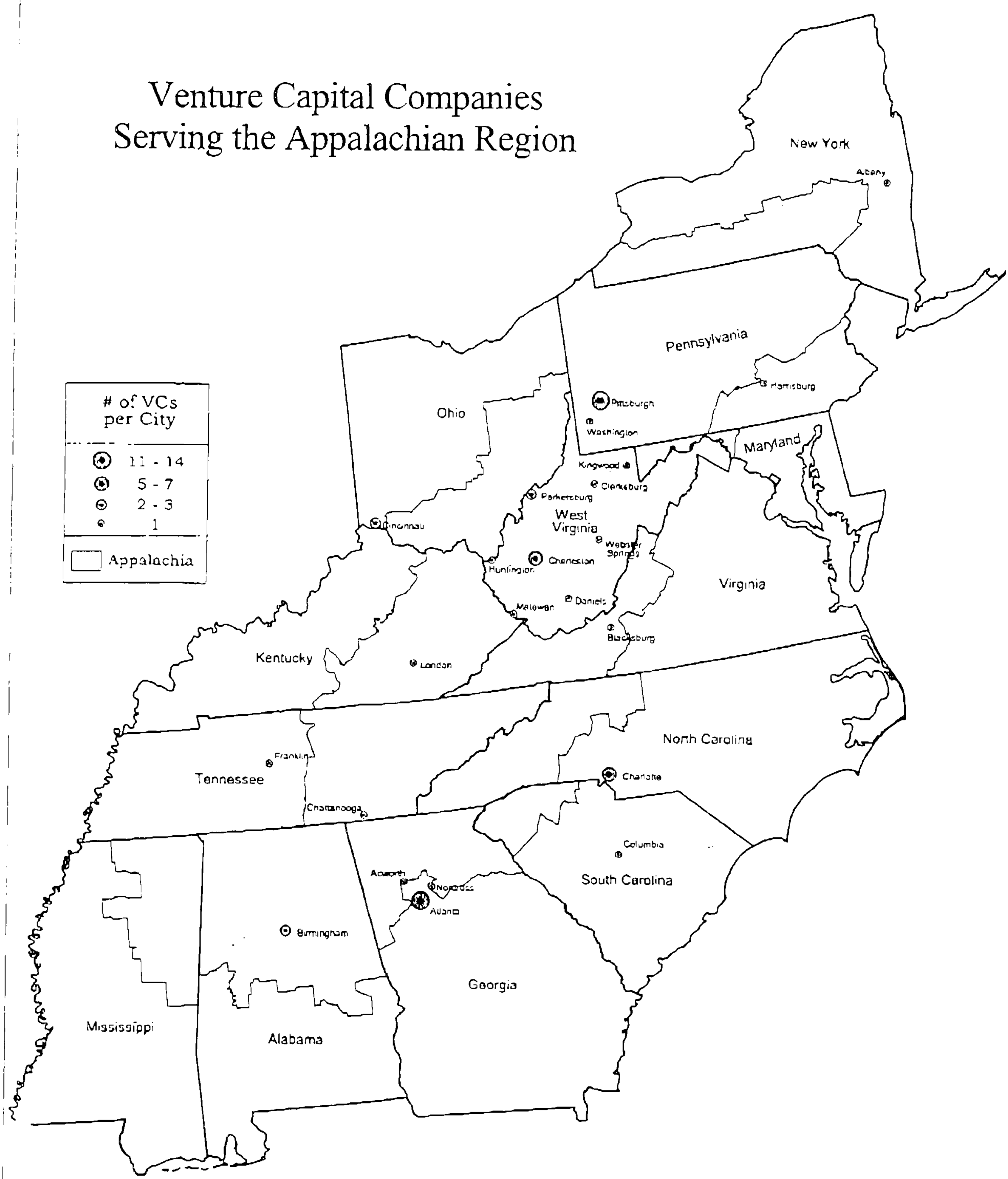
5. Work with state banker associations to examine these new development strategies and find investors to capitalize sub-regional funds

Small Business Investment Companies Serving the Appalachian Region



Data Sources:
U.S. Small Business Administration and Mt. Auburn Associates.

Venture Capital Companies Serving the Appalachian Region



ARC

Data Sources:
U.S. Small Business Administration and Mt. Auburn Associates.

U.S. Small Business Administration

SBA **NEWS RELEASE**

PRESS OFFICE

Release Date: January 15, 1999
Release Number: 99-04

Contact: Mike Stamler (202) 205-6740
Internet Address: www.sba.gov/news/

PRESIDENT CLINTON, SBA OFFER NEW MARKETS INVESTMENT INITIATIVES TO FUEL BUSINESS AND JOB CREATION IN RURAL, INNER CITY AREAS

NEW YORK – President Clinton and U.S. Small Business Administration (SBA) Administrator Aida Alvarez today announced a sweeping new public/private partnership to provide tax credits, investment capital and credit, and technical assistance to stimulate business formation and job creation in economically distressed rural and inner city areas.

The New Markets Initiative could lead to investment of as much as $15 billion in the nation's most economically distressed rural areas and inner cities.

"We have to do more to invest in our own people to give them the tools they need to succeed and to widen the circle of opportunity," the President said.

"Concentrations of poverty and joblessness continue to have a devastating effect on the social and economic fabric of communities across the country, and it is holding America back," the President said. "This lack of opportunity is at the heart of our deepest social divisions. The New Markets Initiative will direct billions of dollars of private and public investment capital and credit into these communities, and go a long way toward opening the doors of opportunity to all Americans."

SBA Administrator Alvarez noted: "It couldn't be more fitting that we are meeting on Martin Luther King's birthday – at the center of economic power in this country – to talk about opening the doors of economic opportunity, to tap into New Markets. Dr. King's words and actions remind us that when we limit economic opportunities for some Americans, we limit the possibilities for all Americans."

The comprehensive program announced today by the President includes participation by the SBA and the Departments of Treasury and Housing and Urban Development, as well as numerous private sector investment and banking professionals and private sector corporate sponsors.

The President and Administrator Alvarez announced the programs today at the Wall Street Project Conference sponsored by the Rev. Jesse Jackson.

The New Markets Initiative is designed to take advantage of attractive business opportunities in underserved rural and inner city communities that are not currently being met. The key elements include: tax credits and loan guarantee incentives, a network of private investment institutions to funnel credit, equity and technical assistance into businesses in America's New Markets, and technical assistance and mentoring programs to help targeted small businesses use new investments to finance growth. The New Markets Initiative includes:

- **New Markets Tax Credits** – To help spur $6 billion in new equity capital for investment in America's New Markets, President Clinton has proposed a tax credit worth up to 25 percent for investments in a wide range of vehicles serving these communities, including community development banks, venture funds and corporations, the new investment company programs listed below, and other targeted investment funds.

- **New Markets Venture Capital Companies (NMVCs)** – NMVCs will be venture capital companies that provide a combination of equity venture capital financing and technical assistance to smaller businesses located in low- and moderate-income (LMI) areas. SBA is proposing a pilot program to create between 10 and 20 NMVCs.

  LMI areas are census tracts where at least 20 percent of the population is beneath the poverty level, or where median family income is less than 80 percent of median family income for the surrounding area. SBA also intends to include other areas in which economic development is lagging, including HUBZones, Enterprise Communities, Empowerment Zones and counties with persistent poverty.

  NMVCs will provide government-guaranteed long-term funding, combined with technical assistance grants, to private for-profit community-based venture capital companies that will target their efforts in these rural and inner city areas. NMVCs must raise at least $5 million in investment capital, which SBA will match up to $10 million for any single NMVC. The interest on the government funding will be deferred for the first five years. NMVCs must also
  obtain commitments to provide at least $1.5 million in technical assistance funding over five years. SBA will provide technical assistance grants amounting to 30 percent of the private capital amount.

  SBA anticipates that the program will involve $100 million in SBA-backed funding and $30 million in technical assistance grants. Establishing the program will require enabling legislation.

- **LMI Investments and Outreach Workshops** – SBA has organized a series of six workshops designed to recruit potential SBIC investors and management teams with experience in investing in small businesses in LMI areas. Beginning in late March, workshops are scheduled for Chicago, Kansas City, New York, Atlanta, Dallas and San Francisco.

  These workshops will result in the creation of new SBIC licensees, new interest in rural and inner city investing, and a database of investment and community development professionals that will be available to work with SBA on this effort.

SBA also will create a new funding mechanism to provide financial incentives to encourage SBICs and Specialized SBICs to invest in LMI areas. The funding will be provided to licensees in amounts that match the level of their investments in small businesses that: 1) are located in LMI areas, or 2) hire at least 35 percent of their workforce from among residents of LMI areas.

- **America's Private Investment Companies (APICs)** – APICs, modeled on the Overseas Private Investment Corporation, will provide equity capital for the creation or relocation of large-scale businesses in inner cities and rural areas. It will fund large, investment partnerships formed by private investors for this purpose. It will be a Department of Housing and Urban Development (HUD) program administered jointly by HUD and SBA to combine SBA's venture investment expertise with HUD's expertise in large scale urban revitalization.

  APICs will be organized as conventional, for-profit private venture capital funds with a minimum private capitalization of $100 million. APICs will be eligible for twice that amount in government guaranties. APIC investments will be required to be in low- and moderate-income areas and require prior government approval for each investment transaction.

  HUD and SBA anticipate that the program will involve $1 billion of government-backed funding. Establishing the program will require enabling legislation.

- **BusinessLINC Initiative** – The BusinessLINC Initiative is a new partnership between the federal government and America's business community to encourage large businesses to work with small business owners and entrepreneurs, especially in America's rural areas and inner cities.

  BusinessLINC, which stands for Learning, Information, Networking, and Collaboration, is designed to stimulate business-to-business relationships that will produce one-on-one technical advice and consulting, classroom and group training, peer group consulting, strategic alliances, and supplier and marketing development for small businesses.

- **New Markets Lending Companies (NMLCs)** – Under this pilot, SBA will select approximately 10 non-depository lending institutions to make SBA-guaranteed loans targeted to New Market small businesses. The proposed NMLC program is a limited term, limited participation pilot that will last between five and 10 years.

  NMLCs will make SBA-guaranteed loans under the 7(a) General Business Loan Guaranty program, the agency's largest financial assistance program. Under the 7(a) program, SBA guarantees up to 80 percent of a loan that is made by a commercial lender to a creditworthy small business that cannot otherwise secure financing on reasonable terms.

  Funding for loan guaranties made under the NMLC initiative will come from the SBA's appropriation for 7(a) program loans, which is funded at a level of $10 billion for the current fiscal year.

U.S. Small Business Administration

Investment Division

Championing America's Entrepreneurs

Existing SBIC Program and Proposed New Markets Equity Investment Programs for Domestic Businesses

COMPARISON OF PROGRAMS

	Key Program Characteristics	America's Private Investment Company Program	Existing SBIC Program	SBIC LMI Investments	New Markets Venture Capital
Investment Focus	Size of Business	Medium to Large	Small	Small	Very Small
	Growth Targets	Leveraged buyouts + financings of major expansions where significant numbers of jobs are created in LMI geographies	Oriented towards very high growth firms, often low tech, whether for later stage or early stage financings	Oriented towards modest growth firms usually low tech, whether for later stage or early stage financings	Serves standard businesses that may not have strong market niches and modest growth prospects, plus service businesses
	Maximum After Tax Profit of Small Enterprise	$25 million (not certain)	$6M	$6M	$2M
	Maximum Net Worth	$75 million (not certain)	$18M	$18M	$6M
	Geographic Restrictions	LMI Zones	Anywhere in U.S. – Limited Foreign	LMI Zones or 35% of employees reside in LMI Zones	LMI Zones
	Employee Requirements	Jobs Created for LMI Persons	None		None

	Key Program Characteristics	America's Private Investment Company Program	Existing SBIC Program	SBIC LMI Investments	New Markets Venture Capital
Business's Management Experience	Experience of Business's Management in Equity Financings	Management, together with fund managers fully understand the investing and management process.	Businesses have some understanding of the process, and can pay consultants, accountants and lawyers to prepare for a financing	Businesses may or may not have some understanding of the process, probably cannot pay consultants, accountants and lawyers to prepare for a financing	Businesses unfamiliar with financing process and cannot pay advisors
	Experience of Business Management in Growing Companies	Experienced to Highly Experienced	Modest Experience to Highly Experienced	Modest Experience	Low Experience
Role of Fund Manager	Financial Technical Assistance Support	Probably Unnecessary	None	None	6% per year of private capital for 5 years
	Assistance by Fund Managers	Fund managers provide mostly strategic assistance, except when in serious trouble and fund managers take over daily management	Fund managers provide mostly strategic assistance, except when in serious trouble and fund managers take over daily management	Businesses require hands on assistance, but not day-to-day involvement by SBIC management.	Businesses require considerable business management assistance both before and after financing
	Control by Fund	No Restrictions	No control except for startups & to rescue investments	"Temporary" control permitted for up to 5 years	No Restrictions
Size and Terms of Invest-ment	Investment Size	Expected investment size: Greater than $50,000,000	Targeted investment size: $300,000 to $5,000,000	Targeted investment size: $150,000 to $1,000,000	Normal expected investment size: $100,000 to $300,000

	Key Program Characteristics	America's Private Investment Company Program	Existing SBIC Program	SBIC LMI Investments	New Markets Venture Capital
	Minimum Term of Investment	No Restrictions	5 years	1 year	No Restrictions
IRRs & Exit Mechanisms	Methods of Achieving IRRs	A principal component of IRR is achieved through sales of equity investments to strategic acquirers or in IPOs	A principal component of IRR is achieved through sales of equity investments to strategic acquirers or in IPOs	Investment returns will usually have to be generated from the business' internal profitability rather than through sale of its equity to third parties	Investment returns will usually have to be generated from the business' internal profitability rather than through sale of its equity to third parties
	Goals of Investors	Market driven (or close to) private risk-adjusted capital	Utilizes market driven private risk-adjusted capital	Utilizes market driven private risk-adjusted capital	IRRs may not be high enough to attract risk-adjusted private capital
Capital Structure & Fees	Minimum Private Capital Requirements	$100M	$5M for debentures, $10M for Participating	Same as SBIC	$5M + $1.5M for Technical Assistance
	Government Role	Government Provided Leverage	Government Provided Leverage	Government Provided Leverage	Government Provided Leverage & Technical Assistance
	Leverage Securities Available	Debentures	Debentures, Participating Securities	Debentures including 10 Year term/ 5 year zero; Participating Securities	Debentures: 10 Year term/ 5 year zero
	Amount of Leverage Possible	Up to 200%	Up to 300%, Approx. $100M Maximum	Up to 300%, Approx. $100M Maximum	Up to 100%, $10M Maximum
	Leverage Rate	Approx. 90 b.p. over 10 Yr. Treasury	Approx. 90 b.p. over 10 Yr. Treasury	Approx. 90 b.p. over 10 Yr. Treasury	Approx. 90 b.p. over 10 Yr. Treasury
	Leverage Fees	*See note following*	1% Commitment Fee, 2% User Fee, 100 b.p. Annual Charge, 50 b.p. underwriting fee	1% Commitment Fee, 2% User Fee, 100 b.p. Annual Charge, 50 b.p. underwriting fee	No fees

	Key Program Characteristics	America's Private Investment Company Program	Existing SBIC Program	SBIC LMI Investments	New Markets Venture Capital
	Management Fees	Maximum management fees of 2.5%, but industry norm is less if funds are larger than $100M in total assets, including leverage	Almost all SBICs are limited to 2.5% of total assets for annual operating expenses	Almost all SBICs are limited to 2.5% of total assets for annual operating expenses	Management fees of up to 8.0% of total assets, per annum
Assets Employed	Annual Program Level	$1.0B	FY99: $1.3B	Included within SBIC Program	$100M (Pilot, not annual)
	Current Outstanding & Committed Government Assets	$1.0B (Projected)	$3.0B	Included within SBIC Program	$100M (Projected) + $30M Technical Assistance
	Total Private & Government Assets	$1.5B (Projected)	$9.0B	Included within SBIC Program	$200M (Projected)
Miscellaneous	Licensing	Contractual Arrangement	Licensed	Licensed	Contractual Arrangement

Notes on leverage fees & subsidy rate in America's Private Investment Company Program: *This program contemplates APICs doing combination mezzanine financing, and equity. Debenture leverage would support the mezzanine portion of investments. Leverage fees would be less than in the SBIC program. Subsidy rate is tentatively pegged at 3.6%.*

COMMUNITY DEVELOPMENT VENTURE CAPITAL FUND INVESTORS

These corporations have invested in community development venture capital funds.

1 ABC, Inc.
2 American State Bank
3 Androscoggin Savings Bank
4 AT&T Corp.
5 Bank of New York Co., Inc. (The)
6 Bank of Yazoo City
7 BankBoston
8 Bankers Trust Company
9 Bath Savings Institution
10 Bear Stearns Companies, Inc. (The)
11 Bell Atlantic
12 Blackstone Group, L.P. (The)
13 Boston Edison
14 Boston Safe Deposit & Trust
15 Calvert Social Investment Fund
16 CBS Corporation
17 Central Bank – Monroe
18 Chase Manhattan Corporation (The)
19 CIBC Oppenheimer
20 Citibank
21 Concordia Bank & Trust Company
22 Consolidated Edison Company of New York
23 Corestates Bank
24 Credit Suisse/First Boston
25 Deloitte & Touche LLP
26 Deposit Guaranty National Bank
27 Dime Bancorp
28 Donaldson, Lufkin & Jenrette
29 Estee Lauder Companies Inc.
30 Farmers Bank & Trust Company
31 Fidelity Investments
32 First National Bank of Commerce
33 First National Bank of Phillips County
34 First Union
35 Fleet Bank, N.A.
36 General Electric Company
37 Goldman, Sachs & Co.
38 Hibernia National Bank
39 Independence Savings Bank
40 J.P. Morgan & Co. Inc.
41 Kennebunk Savings Bank
42 Key Bank of Maine
43 Loews Corporation
44 Magellan Health Services, Inc.
45 Merchants & Farmers Bank
46 Merrill Lynch L.P. Holdings Inc.
47 Metropolitan Life Insurance Company
48 Morgan Stanley & Dean Witter & Co.
49 Nations Bank
50 NCB Development Corporation
51 New York Life Insurance Company
52 Ocean National Bank
53 PaineWebber Group Inc.
54 Peoples Heritage Bank
55 Pepperell Trust Company
56 Pfizer Inc.
57 Planters Bank & Trust Company
58 PNC Bank
59 Primedia Inc.
60 Reader's Digest Association, Inc. (The)
61 Simmons First National Bank
62 State Street Bank
63 Tiffany & Company
64 Time Warner Inc.
65 Travelers Group
66 Trustmark National Bank
67 Union Planters Bank of NW Mississippi
68 USTrust and United States Trust

compiled by Julia Rubin, Harvard University

APPALACHIAN REGIONAL COMMISSION
A Proud Past, A New Vision

Community Development Venture Capital (CDVC)
Fund Examples

Prepared by Julia Rubin, Harvard University

The CDVC industry is a relatively new one. The oldest fund was created in 1969, and most funds currently in existence were founded less than 10 years ago.

The first CDVCs were Title VII community development corporations, created in the late 1960s and 1970s to empower residents of distressed communities and help alleviate poverty. They received federal grants to engage in a broad range of activities, including business and economic development, training, and housing and community development. As part of their business and economic development missions, a number of the CDCs began their own business ventures, or invested some of their assets in ventures owned by entrepreneurs in the community.

Two of the five CDVCs profiled below -- Kentucky Highlands Investment Corporation and Coastal Ventures Limited Partnership -- originated through the Title VII program.

- **Kentucky Highlands Investment Corporation (KHIC)**

KHIC is a private, non-profit 501 (C)(4) corporation organized in 1968 to pursue economic development in eastern Kentucky. 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 its region. These include subordinated and collateralized debt, equity, real-estate construction and management and management consulting services.

Kentucky Highlands invests in businesses located in its target area, or which are willing to move there. The fund carries out its services through the parent organization, and a number of wholly owned for-profit and nonprofit subsidiaries, such as Mountain Ventures, a Small Business Investment Company.

- **Coastal Ventures**

Coastal Enterprises, Inc. (CEI) is a nonprofit community development corporation, founded in 1977 to "help Maine's people and communities, particularly those with low incomes, reach an adequate and equitable standard of living and working" (CEI, 1997). CEI provides financial and technical assistance to small businesses, and housing and social service providers.

As part of its economic development activities, CEI has provided equity financing to small businesses since the mid-1980s. In 1996, CEI launched a for-profit subsidiary, Coastal Enterprises Limited Partnership Ventures (CLPV), to focus exclusively on developmental equity. CLPV is currently a $5.5 million dollar community development venture capital fund. The fund was capitalized with investments from a number of Maine banks, several national foundations, and the parent entity, Coastal Enterprises, Inc. CEI serves as the general partner for CLPV.

- **Minnesota Investment Network Corporation**

In the 1980s and early 1990s, many states followed the federal government's example and initiated state-based developmental equity efforts. The Minnesota Investment Network Corporation was created by the Minnesota legislature in 1991, to support the start-up and development of technology-based small and medium sized manufacturers, primarily in rural Minnesota.

In 1996, the fund ran out of capital and was forced to stop investing. MIN-Corp's management convinced the state legislature to allow the fund to convert to a private nonprofit structure, thus increasing its independence and ability to attract additional sources of capital. The $7.5 million that MIN-Corp received from the state must be invested in Minnesota, with 80% of it placed in the rural portions of the state.

- **Northeast Ventures**

The concept for Northeast Ventures emerged in 1985, following a series of meetings to discuss strategies for countering the economic devastation brought to northeastern Minnesota by the decline of the U.S. steel industry. The president of the region's preeminent law firm used the meetings to advocate for a community development venture capital fund to help jump-start the region's economy. In 1987, Northeast Ventures was launched as a for-profit corporation, under his leadership. The fund 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.

Northeast Ventures is structured as a for-profit corporation. It invests primarily in Northeastern Minnesota, with the option of placing up to 15% of fund assets in other parts of the state.

- **New York Community Investment Company**

The New York Community Investment Company (NYCIC) was created in 1996 by a consortium of New York City commercial banks. The banks set up and capitalized the for-profit limited liability corporation with $10 million, to help meet their federal Community Reinvestment Act obligations, and to identify potential future lending opportunities.

NYCIC's mission is to provide equity and subordinated debt to companies that range from start-ups to $20 million in sales, and which 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. NYCIC also is interested in providing funds for community-based organizations and for nonprofit-sponsored businesses.

Albert Brown [illegible] [illegible] [illegible] since '99
V P office [illegible] in Congress

Tracy Carter – Office of Public Service
Presidential Accounts

Briefing

Back office
McDow Cathy

reputation [illegible] [illegible] program
[illegible] positive effort

Gary Wald by Big Jack
Lobbying effort

AMERICA'S PRIVATE INVESTMENT COMPANIES

In the six years since President Clinton took office, the economy has created nearly 17.7 million new jobs. Yet even during one of the greatest periods of sustained economic growth in American history, we still have not achieved true equality of opportunity. Concentrations of poverty and joblessness continue to have a devastating effect on the social and economic fabric of communities across the country. This lack of opportunity is at the heart of our deepest social divisions.

The evidence strongly suggests that there are attractive business opportunities in underserved inner city and rural communities that are not being met. Among the most critical needs of these communities is access to substantial equity-type investment and quality employment opportunities.

The President's New Markets Initiative is designed to make it more attractive to invest in these communities and ensure that the opportunity to stimulate job growth, neighborhood and economic development of America's untapped new markets is not lost.

The America's Private Investment Company (APIC) initiative is a key component of the president's New Markets Initiative. It complements SBA's equity investment programs, encouraging substantial business expansion into inner cities and rural areas.

America's Private Investment Companies
This new program will provide equity capital for larger-scale businesses in inner cities and rural areas. It will fund large, investment partnerships formed by private investors for this purpose. It will be jointly administered by the Department of Housing and Urban Development (HUD) and SBA to combine SBA's venture investment expertise with HUD's expertise in large scale urban revitalization.

A number of market expansions and large start-ups could be focused to serve low-and-moderate income areas if appropriate financial tools were available. APICs will be organized as for-profit private capital funds with certain minimum equity capitalization. APICs will be eligible for twice that amount in Government guaranties on loans obtained from private sources. A $100 million initial equity commitment would leverage $200 million in government-guaranteed debt, creating a $300 million fund. These significant pools of investment capital will be available to take advantage of the opportunities described above and will help to create quality employment opportunities in inner cities and rural areas.

HUD and SBA will jointly solicit proposals for the creation of the investment partnerships. Approximately five organizations will be selected. APIC investments must be in low- and moderate-income areas and otherwise conform with the APIC program's public policy objectives.

HUD/SBA anticipate that the budget authority authorized in FY 2000 will provide $1 billion of government-backed funding at a budget cost of $37 million. Combined with a private capital investment of $500 million, the program would have a total impact of $1.5 billion per year.

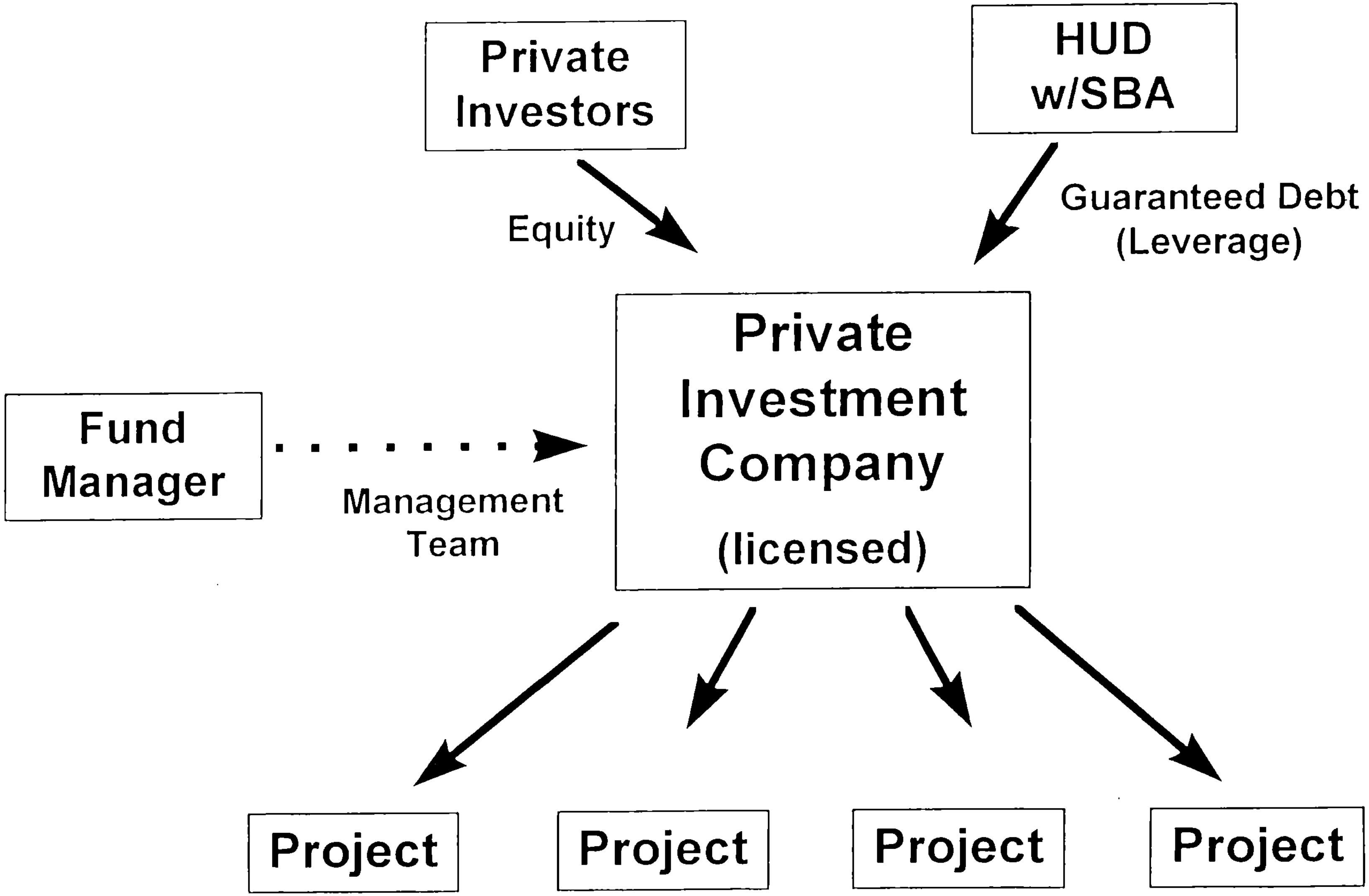
New Markets Initiative

America's Private Investment Companies

U.S. Department of Housing and Urban Development

1999

How the APICs Will Work



Overview: Goals and Need

APIC Adapted from:

SBA's Small Business Investment Companies

APIC Created to:

- Expand private investment in large-scale businesses in LMIs.
- Reach untapped markets in urban and rural areas.
- Complement HUD's existing programs for large-scale revitalization.
- Enable a wide variety of project types, including commercial real estate.

APIC: Long-term Capital Targeted to Development Needs

- Direct investments in active businesses
- "Patient capital" -- long-term equity and debt
- Eligibility for New Markets Tax Credit

Borrowing with Government Guarantee

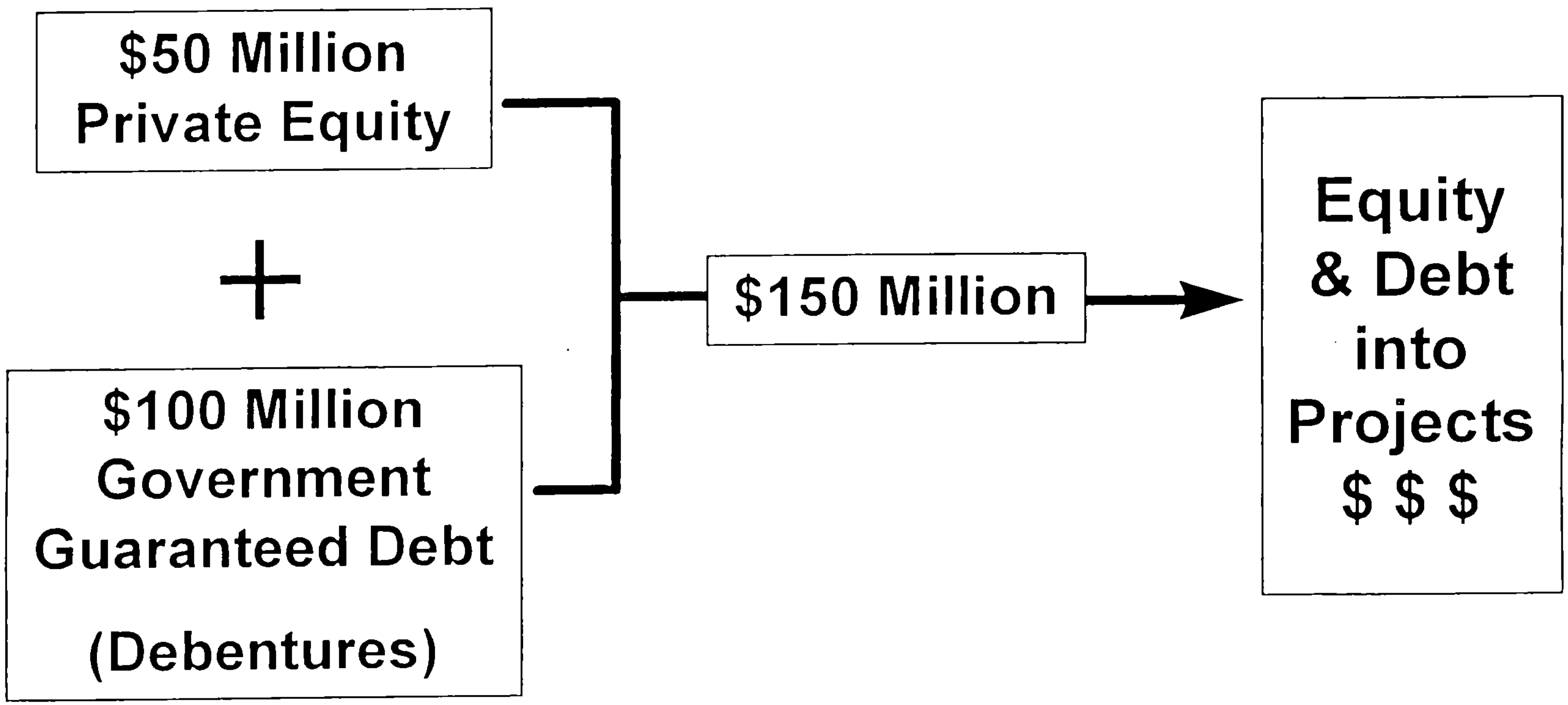
- The Government will guarantee APIC debentures up to 2 times an APIC's equity

- The borrowed money must be invested in LMIs

- Borrowing at low Government-guaranteed rates increases returns for equity investors

APIC: Basic Numbers

Example



Scale

- **$36M in credit subsidy leverages $1 billion in private loans and $500M in private equity** ($1.5 billion per year)

- **APIC will create large investment companies** (expected $75 - 450M) **able to fund large projects** (expected $5 - 50M)

Risk Mitigation

Private Investors as APIC's Equity Shield

- Private equity is fully at risk and is <u>not</u> guaranteed by Government

- Private equity serves as a shield to Government-guaranteed debt:
  - safeguarding Government credit subsidy
  - protecting the U.S. Taxpayers from losses

- Every cent of private investment must be lost before Government faces any losses

The Investors

<u>Broad Array Eligible</u>:

- **Corporations**
- **Insurance Companies**
- **Banks** (eligible for CRA credit)
- **Pension Funds**
- **"Social Investors"**
- **Other Individual and Institutional Investors**

Selecting Experienced Fund Managers

Team Qualifications:

- Proven track record in direct equity investment and portfolio management
- Demonstrated ability to raise capital from private investors
- Experience in community development settings

Ensuring Financial Soundness and Rewarding Performance

- Financial Soundness Review
- Performance Review
  - Local hiring, quality jobs, other community benefits target by APICs themselves
- High performers eligible for more favorable financing

CREDIT BUDGETING AT A GLANCE

Federal Credit Reform Act of 1990

- changed the budgetary treatment from cash to NPV
- enabled cost comparison between direct loans, loan guarantees, and grants
- required budgeting for the subsidy cost of loans and guarantees

Subsidy cost

- Net present value of all cashflows to and from the Government discounted to date of disbursement, expressed as a percentage of program volume (subsidy rate)
- Cashflows may include: principal and interest, fees, defaults, recoveries on default, prepayments, penalties, and other payments/collections. Also need information on timing of payments/collections.
- Cashflows do NOT include administrative costs
- Cashflows developed by agencies, approved by OMB, using technical assumptions based upon historical program experience (or reasonable proxy) and economic assumptions for President's Budget
- Agencies must use subsidy rate published in the President's Budget for the applicable fiscal year (unless program specifics enacted are different than those assumed in Budget, e.g. new program proposal altered by Congress)

What happens when we're wrong

- Agencies reestimate subsidy cost periodically
- Reestimates paid for through permanent appropriation, not out of agencies' discretionary appropriation
- Agencies are expected to incorporate new information into future subsidy rates

New program difficulties

- Finding a reasonable proxy, or working with no data
- Assumptions about borrower behavior
- Assumptions about program operation

Yvette Dennis
today used for Courtney

BRD:CBT
5/6/99

Illustrations of Potential APIC Investments

This chart lists businesses that would benefit from investments and loans provided by APICs. Each category also lists a few real-world examples, drawn predominantly from the Chicago marketplace, and some hypothetical examples.

Possible Investments	**Investment Structure / Involved Parties**	**Capital Markets Need**
Large company opens a new facility • Data processing back office • Allen Edmonds call center • Tootsie Roll new factory • Chicago Tribune Liberty Center • Bank retail branch	Existing company New division, subsidiary or a financial joint venture	Inducement to locate
Mid-size manufacturing company expands existing facility/campus or upgrades its equipment • A. Finkel & Sons Forging • A-Wire powder coating	Existing company	Offsetting costs
Buyout a division/factory of a large company, and re-vitalize company in current facility • Brach's Candy (possible, not actual) • Helene Curtis facility • Inner City hospitals	New legal entity or a financial joint venture Existing management, ESOP, or new investor-management team	Inducement to stay
Buy real estate of a departing large company, convert to business incubator or industrial park. • Sunbeam (now SunGate Park) • Fulton-Carroll Incubator • Stockyards meatpacking plants (now Back of the Yards Industrial Park)	New entity, or developer or may involve nonprofit	Capital markets gap
Joint venture of a large and small company to create new entity • Hispanic Manufacturing • Trumark - Macke Automotive	New legal entity (may or may not own real estate)	Offsetting costs
Brownfields Clean-up, re-use and sale • Cherokee Investment Fund • Land Bank • Schwinn Bicycle Factory	Specialized investment funds or separate legal entity, perhaps with nonprofit	Capital markets gap

Mid-size service company expanding in targeted area • Home health care / nursing • Building contractor • Trucking company • Rachel's Bus Company	Existing company	Offsetting costs, market gap
Multi-tenant shopping center real estate development • Jeffrey Plaza • Back of the Yards • Gateway • Bed-Stuy Pathmark	Developer	Offsetting costs
Single-user Retail • Magic Johnson Movie Theaters • Home Depot • Walgreen's	Developer or real estate arm of company	Offsetting costs
Expand retail chain as tenant • company stores (Foot Locker, Payless Shoes, Red Lobster, Bakers' Square) • franchises/coops (fast food, automotive repair, hardware stores)	Existing company (or subsidiary) or through sub-franchisee	Offsetting costs
Single-site retail (probably too small for APIC)	Existing company	Offsetting costs

Investment Division

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Fax

To: Sarah Rosen	**From:** Saunders Miller
FAX: 202-456-2223	**FAX:** 202-205-6013
Voice:	**Voice:** 202-205-3646
Date: 1/14/99	**No. of Pages Including Cover:** 5

Message:

Enclosed is the latest copy of the program comparison chart which I am also emailing, but just in case it doesn't open properly, here's a fax copy..

Investment Division

Existing SBIC Program and Proposed New Markets Equity Investment Programs for Domestic Businesses

COMPARISON OF PROGRAMS

	Key Program Characteristics	America's Private Investment Company Program	Existing SBIC Program	SBIC LMI Investments	New Markets Venture Capital
Investment Focus	Size of Business	Medium to Large	Small	Small	Very Small
	Growth Targets	Leveraged buyouts + financings of major expansions where significant numbers of jobs are created in LMI geographies	Oriented towards very high growth firms, often low tech, whether for later stage or early stage financings	Oriented towards modest growth firms usually low tech, whether for later stage or early stage financings	Serves standard businesses that may not have strong market niches and modest growth prospects, plus service businesses
	Maximum After Tax Profit of Small Enterprise	$25 million (not certain)	$6M	$6M	$2M
	Maximum Net Worth	$75 million (not certain)	$18M	$18M	$6M
	Geographic Restrictions	LMI Zones	Anywhere in U.S. – Limited Foreign	LMI Zones or 35% of employees reside in LMI Zones	LMI Zones
	Employee Requirements	Jobs Created for LMI Persons	None		None

	Key Program Characteristics	America's Private Investment Company Program	Existing SBIC Program	SBIC LMI Investments	New Markets Venture Capital
Business's Management Experience	Experience of Business's Management in Equity Financings	Management, together with fund managers fully understand the investing and management process.	Businesses have some understanding of the process, and can pay consultants, accountants and lawyers to prepare for a financing	Businesses may or may not have some understanding of the process, probably cannot pay consultants, accountants and lawyers to prepare for a financing	Businesses unfamiliar with financing process and cannot pay advisors
	Experience of Business Management in Growing Companies	Experienced to Highly Experienced	Modest Experience to Highly Experienced	Modest Experience	Low Experience
Role of Fund Manager	Financial Technical Assistance Support	Probably Unnecessary	None	None	6% per year of SBA's leverage for 5 years
	Assistance by Fund Managers	Fund managers provide mostly strategic assistance, except when in serious trouble and fund managers take over daily management	Fund managers provide mostly strategic assistance, except when in serious trouble and fund managers take over daily management	Businesses require hands on assistance, but not day-to-day involvement by SBIC management.	Businesses require considerable business management assistance both before and after financing
	Control by Fund	No Restrictions	No control except for startups & to rescue investments	"Temporary" control permitted for up to 5 years	No Restrictions
Size and Terms of Invest-ment	Investment Size	Expected investment size: Greater than $50,000,000	Targeted investment size: $300,000 to $5,000,000	Targeted investment size: $150,000 to $1,000,000	Normal expected investment size: $100,000 to $300,000
	Minimum Term of Investment	No Restrictions	5 years	1 year	No Restrictions

	Key Program Characteristics	America's Private Investment Company Program	Existing SBIC Program	SBIC LMI Investments	New Markets Venture Capital
IRRs & Exit Mechanisms	Methods of Achieving IRRs	A principal component of IRR is achieved through sales of equity investments to strategic acquirers or in IPOs	A principal component of IRR is achieved through sales of equity investments to strategic acquirers or in IPOs	Investment returns will usually have to be generated from the business' internal profitability rather than through sale of its equity to third parties	Investment returns will usually have to be generated from the business' internal profitability rather than through sale of its equity to third parties
	Goals of Investors	Market driven (or close to) private risk-adjusted capital	Utilizes market driven private risk-adjusted capital	Utilizes market driven private risk-adjusted capital	IRRs may not be high enough to attract risk-adjusted private capital
Capital Structure & Fees	Minimum Private Capital Requirements	$100M	$5M for debentures, $10M for Participating	Same as SBIC	$5M + $1.5M for Technical Assistance
	Government Role	Government Provided Leverage	Government Provided Leverage	Government Provided Leverage	Government Provided Leverage & Technical Assistance
	Leverage Securities Available	Debentures	Debentures, Participating Securities	Debentures including 10 Year term/ 5 year zero; Participating Securities	Debentures: 10 Year term/ 5 year zero
	Amount of Leverage Possible	Up to 200%	Up to 300%, Approx. $100M Maximum	Up to 300%, Approx. $100M Maximum	Up to 100%, $10M Maximum
	Leverage Rate	Approx. 90 b.p. over 10 Yr. Treasury	Approx. 90 b.p. over 10 Yr. Treasury	Approx. 90 b.p. over 10 Yr. Treasury	Approx. 90 b.p. over 10 Yr. Treasury
	Leverage Fees	*See note following*	1% Commitment Fee, 2% User Fee, 100 b.p. Annual Charge, 50 b.p. underwriting fee	1% Commitment Fee, 2% User Fee, 100 b.p. Annual Charge, 50 b.p. underwriting fee	No fees

	Key Program Characteristics	America's Private Investment Company Program	Existing SBIC Program	SBIC LMI Investments	New Markets Venture Capital
	Management Fees	Maximum management fees of 2.5%, but industry norm is less if funds are larger than $100M in total assets, including leverage	Almost all SBICs are limited to 2.5% of total assets for annual operating expenses	Almost all SBICs are limited to 2.5% of total assets for annual operating expenses	Management fees of up to 8.0% of total assets, per annum
Assets Employed	Annual Program Level	$1.0B	FY99: $1.3B	Included within SBIC Program	$100M (Pilot, not annual)
	Current Outstanding & Committed Government Assets	$1.0B (Projected)	$3.0B	Included within SBIC Program	$100M (Projected) + $30M Technical Assistance
	Total Private & Government Assets	$1.5B (Projected)	$9.0B	Included within SBIC Program	$200M (Projected)
Miscellaneous	Licensing	Contractual Arrangement	Licensed	Licensed	Contractual Arrangement

Note on leverage fees & subsidy rate in America's Private Investment Company Program. *This program contemplates doing combination mezzanine financing,, and equity. Debenture leverage would support the mezzanine portion of investments. Leverage fees would be less than in the SBIC program. Subsidy rate is tentatively pegged at 3.6%..*

A Small Business Investment Company (SBIC) Success Story

Minority-owned

TLC Next Generation International Holdings LLC
St. Louis, Missouri

TLC Next Generation is the largest distributor of wireless communications products (including cellular and digital phones, pagers, and related equipment) in the St. Louis metropolitan area. Leroy Wright, the company's founder and CEO, created TLC Next Generation in 1997 by combining two St. Louis cellular phone distributors: Wright's own company, Wright Cellular, serving business customers in downtown St. Louis; and Next Generation, a 15-store chain of Southwestern Bell Wireless (SBC Communications) retail outlets in suburban shopping malls. The combined company now employs 77 people.

Leroy Wright, at age 28, is the first African American in St. Louis to accomplish this type of multimillion dollar acquisition. Wright says he hopes to become St. Louis' first Black-owned firm traded publicly on the stock exchange. A native of St. Louis, Wright was raised by his grandparents, both of whom were blind. Wright's grandfather had his own business selling brooms and washcloths door-to-door. Leroy often went along, learning from an early age how to be a salesman. "My grandfather would say to me, 'Look what I'm doing, and I'm blind! Just imagine what you can do," Wright recalls.

It was as a salesman in 1996 that Leroy Wright found his lead investor for the creation of TLC Next Generation. Byron Winton needed a phone. He had just arrived in St. Louis to manage the newly formed Civic Ventures Investment Fund, a multimillion dollar fund established by a group of Fortune 500 companies to provide capital as well as management and financial advisory services for small businesses, particularly minority-owned companies, in St. Louis and the Midwest. Winton went to Wright Cellular and struck up a conversation with Leroy Wright. The two businessmen kept in touch over the next year, during which time Civic Ventures became a federally licensed small business investment company (SBIC) and Wright Cellular became the fourth largest seller of cellular phones in the region.

Byron Winton recalls: "Wright was doing well with his small business, but he didn't really want to settle for fourth place. I said, 'Why not play to win?'" With backing from Civic Ventures, Wright decided to purchase Next Generation, Inc., his main competition and a much larger company. Wright and his wife were willing to invest everything they had in the deal. Civic Ventures could finance a portion ($1 million) of the purchase price, but Wright needed other investors. He went to every major bank in town, but they all turned down his proposal. "It seemed like a 'mission impossible' for a while," says Winton.

Then, at a business conference in Baltimore, Wright met Elyn Dortch, a senior vice president of NationsBank in North Carolina. NationsBank had just purchased Boatmen's Bank, one of the St. Louis banks that had rejected Wright's loan request. Dortch, intrigued with Wright's plan, called a bank colleague in St. Louis and urged him to reconsider Wright's proposal. Two months later, NationsBank agreed to provide a package of senior debt and capital to help finance the deal, including a venture capital investment of $500,000 from NationsBanc SBIC Corporation, a small business investment company that focuses on minority and woman-owned businesses and on providing venture capital for community development purposes.

Wright credits his financial partners with making the acquisition a reality: "The deal was able to get done because of the proactive involvement of NationsBank and Civic Ventures," Wright says. "They've exhibited the kind of progressive thinking that's needed today to support minority entrepreneurship in St. Louis." 3/5/98

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A Small Business Investment Company (SBIC) Success Story

Minority-owned

Midwest Stamping and Manufacturing Company
Bowling Green, Ohio

Midwest Stamping and Manufacturing Company produces medium and heavy gauge metal components (known in the industry as "stampings") that are integral parts of the bodies and frames of automobiles. Many of the world's leading auto manufacturers, including Ford, Honda, Mercedes, Nissan, Saturn, and Mazda, use Midwest products. Both Honda and Saturn have presented Midwest with awards for product quality.

The company's CEO, Ronald Thompson, purchased Midwest Stamping and Manufacturing Company in March, 1993, with financial backing from a specialized small business investment company, TSG Ventures, in Stamford, Connecticut. TSG's principals, Duane Hill and Cleveland Christophe, had known Thompson for years and had worked with him in a previous business transaction. Confident in the entrepreneur's abilities, TSG Ventures invested $2 million to enable Thompson to acquire Midwest Stamping and Manufacturing.

At the time of the acquisition in 1993, Midwest had revenues of $64 million and employed 320 people. By the end of 1996, revenues had grown to $108 million. Today, Midwest employs over 600 people. Most work at the company's two Ohio plant facilities in Bowling Green and Edgerton. In addition, Midwest employs about 100 people at its plant in Sumter, South Carolina and 10 people in Dearborn, Michigan. In 1998, the company plans to open a plant in Springfield, Kentucky, and hire another 100 employees.

Thompson believes TSG Ventures has played an important role in his company's success:

> "Before I acquired Midwest Stamping and Manufacturing Company, I was in the business of manufacturing railroad and defense materiel. The equity financing from TSG was important originally in structuring the acquisition transaction because it gave me credibility as I entered a new industry. We had our own equity, but having institutional equity investors added to our credibility. TSG was also helpful in negotiating terms of our senior and subordinated credit agreements. Since the acquisition, they've helped us evaluate strategic opportunities that have presented themselves. TSG has provided not only capital resources, but access to a very valuable network of human resources as well."

According to Duane Hill, President of TSG Ventures:

> "The Midwest Stamping investment is an excellent example of how a small business investment company (SBIC) can start early on with an entrepreneur and grow with him, providing financial and strategic advice. It's a classic case of what the SBICs were created to do."
> 12/9/97

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A Small Business Investment Company (SBIC) Success Story

woman-owned

The Merchandising Group (TMG)
New York City, NY

TMG is a woman-owned and managed company that provides field marketing support for Fortune 500 manufacturers of consumer products. TMG employs 110 full-time and 4,500 part-time staff who work on an assignment basis to introduce products to retailers all over the country. The permanent cadre of full-time staff can be expanded quickly with part-time staff as needed.

The senior management of TMG includes:

- Carol Atwood, President. Atwood has 20 years' experience working in retail marketing. She started with TMG in 1983 and became President in 1988.
- Diane Teigen, Executive Vice President for Sales. Teigen has worked in retail for over 25 years and started with TMG in 1977.
- Carole Crist, Executive Vice President for Operations, joined TMG in 1976.
- Susan Kiernan, Vice President for Sales and Marketing, joined TMG in 1990 after working with NYNEX and Communispond.

TMG is part of the rapidly growing $1 billion field marketing industry. TMG sets itself apart from competitors with advanced on-line reporting systems, a proprietary field performance quality control process, and a high retention rate of experienced people. The company was started in 1947; the current management group acquired the company in 1990 and has more than doubled the company's annual sales.

Sterling Commercial Capital, a small business investment company (SBIC) licensed in 1988, has provided $500,000 in financing to TMG for working capital to support its expansion. This is one half of the $1 million in financing TMG will use this year to meet its current growth requirements. The other half comes from New York Community Investment Company LLC, a non-SBIC investment company owned by a number of major NYC banks.

TMG's management welcomes input from Sterling in connection with their long-range business plan. Sterling's President, Harvey Granat, considers this company to be an emerging success story because TMG has "an enlightened management group." According to Granat, "They're enterprising, well-organized. They're sticklers for operating in accordance with a business plan, making projections, and going by the numbers. They take great pride in the professionalism of all the people they employ. This pride starts from the top."

4/15/97

A Small Business Investment Company (SBIC) Success Story

Woman-owned

Mothers Work, Inc.
Philadelphia, PA

Mothers Work is a national retailer of maternity clothing designed for career women. The company operates about 545 locations nationwide in 46 states and employs approximately 3,000 people. Revenues in fiscal 1996 were $199 million. In 1995, Mothers Work was recognized as Portfolio Company of the Year by the National Association of Small Business Investment Companies (NASBIC).

Mothers Work was established in 1980 by Rebecca Matthias, who realized (with the pending birth of her first child) that attractive maternity clothing suited to the needs of successful career women was hard to find. Seeing an untapped market, Matthias bought some executive maternity clothing wholesale on Seventh Avenue in New York City and tried to market her merchandise with a catalog. She sent out thousands of catalogs, but sold almost nothing. The result: a net loss of $6,500 and a closet full of maternity clothes. Rather than give up, Matthias decided to call everyone who had requested catalogs but had not placed orders to find out what it was they needed that she didn't have. What she learned led her to begin manufacturing her own products.

Limited capital for expansion led to franchising as a way to grow the business. The success of the franchises gave Matthias the funds she needed to open the first company-owned "test store." In December 1988, the first institutional investor in Mothers Work was a small business investment company (SBIC), Meridian Venture Partners, which provided a $250,000 loan with equity features. At that time, Mothers Work had about 75 employees. In June 1990, Meridian provided another $300,000 loan. Meridian's investment attracted other venture capital sources, enabling Mothers Work to expand its business, in part by buying back the franchises and converting them into company-owned stores. By 1992, when Meridian made its next investment in Mothers Work, the company had grown from 75 to nearly 300 employees.

From 1988 until Mothers Work went public in 1993, Meridian Venture Partners invested over $2.2 million in the company, providing the "patient," long-term capital Matthias needed to grow her company. "Patient capital is critical in a startup company," says Matthias. "A company doesn't grow in a straight line going from the bottom left to the top right of the growth chart." The initial public offering enabled Mothers Work to improve manufacturing technology. By 1995 Mothers Work had acquired three other maternity apparel companies--Page Boy, A Pea In The Pod, and Motherhood Maternity Shops--adding over 300 stores. Matthias is emphatic about the important role the SBIC played in her company's success:

> "I had no experience. I had no capital. I really had no company. I had an idea. And if it hadn't been for the investment from an SBIC, that's where I'd still be."

3/12/97

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A Small Business Investment Company (SBIC) Success Story

Rusnak

NuCo2, Inc.
Stuart, Florida

NuCo2, Inc. is the country's leading supplier of liquid or "bulk" carbon dioxide (CO2) used by retail establishments to carbonate and dispense fountain beverages. Supplying CO2 in liquid form is a relatively new and convenient alternative to the traditional method of supplying CO2 in its gas form, which must be transported and stored in unwieldy 50-pound high-pressure cylinders. NuCo2 "takes its customers out of the CO2 business" by installing a stationary CO2 storage system on the customer's premises and keeping it filled with liquid CO2. Under this arrangement, the customer leases the CO2 storage system from NuCo2. Some customers own their own tanks and contract with NuCo2 to supply the CO2.

NuCo2 today has 30,000 accounts in more than 30 states. Major customers include McDonald's, Pizza Hut, Kentucky Fried Chicken, Burger King, Wendy's, Hardees, Subway, Shoney's, Chili's, 7-Eleven, AMC Theaters, Universal Studios, and Walt Disney World. Its headquarters remains where the company began, in Stuart, Florida, about 50 miles north of West Palm Beach.

Stuart has a population of about 17,000. With 210 employees nationwide and 71 in Stuart, NuCo2 is a major employer in this rural community. Even though business now extends throughout the eastern United States, the chief executive officer, Ed Sellian, has no intention of moving the company headquarters. Says Sellian:

> We want to be a large company with a hometown flair. In a small community, the work ethic is different. We try to keep a family atmosphere in the workplace. There's creativity in that kind of atmosphere. People want to work here—they appreciate the way they're treated.

In May 1992, NuCo2 had 14 employees and had installed 700 tanks. All the company's business at that time was in the state of Florida. Revenues were less than $1 million. Ed Sellian had bigger plans for his company, but he needed financing. Three small business investment companies (SBICs), led by Argentum Capital Partners, provided $1.5 million. According to Sellian, the SBIC funds were crucial:

> The banks and other lending institutions didn't really understand our business model or plan. We had a new concept. The banks had a hard time relating to a business whose assets were spread out, rather than all in one place. We wouldn't have been able to get as far as we did, to become a public company, without the small business investment companies.

With adequate financing in place, NuCo2 was able to expand its customer base dramatically and in December 1995 held a successful initial public offering. The company now generates annual revenues of about $20 million. 6/17/97

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Rural

A Small Business Investment Company (SBIC) Success Story

Douglas Machine
Alexandria, Minnesota

Douglas Machine manufactures equipment for specialty packaging. Every household in America has products that have been packaged by Douglas Machine. Many of the largest U.S. producers of foods, beverages, and consumer products use Douglas machines at the end of their assembly lines to put packaged products into cardboard shipping cases. The company is named for the county in which it is located--Douglas County, population 30,000--about 100 miles northwest of Minneapolis. With 550 employees, Douglas Machine is the county's largest employer.

Brothers Vern and Paul Anderson and their cousin, Arnold Thoen, founded Douglas Machine in 1966. Vern and Paul had worked for Thiele Engineering in Minneapolis, selling customized packaging equipment. Arnold had a farm machinery repair shop which became Douglas Machine shortly after Vern joined the operation. From this modest beginning, Douglas Machine grew quickly to become a major player in the case packing industry. By 1986, the company had 270 employees and $11.3 million in sales. That year the owners decided to sell the company to APV, an international conglomerate based in the United Kingdom. Douglas Machine continued to operate much as in the past, but with access to the resources of a large parent company. Vern and Paul Anderson continued as senior managers.

By 1993, sales had grown to $28.6 million and Douglas Machine employed about 320 people. However, the Andersons were concerned about changes occurring at APV and decided to try to buy back their company and return it to local control. Their search for an equity partner led them to the Minneapolis-based small business investment company (SBIC), Norwest Venture Capital. With $11 million in financing from Norwest, the Andersons were able to acquire Douglas Machine from APV in December 1993.

"The people at Norwest had good insight about what to expect when acquiring a company," says Vern Anderson. "They helped us negotiate with the banks and set up a strategic plan." Norwest had rights to two board seats at Douglas Machine. "We had gotten to know the folks at Norwest," Anderson recalls. "When it was time to decide who would sit on our board, they let us choose who we wanted." Anderson has been impressed with the board members from Norwest, John Whaley and Steve Sefton. "They take a long-range view," he observes. "They're not short-sighted about facilities improvements like some stockholders. They think about what's best for the company down the road."

Since the buy-out, the company's performance has steadily improved. Revenues in 1996 were $48 million. For 1997, revenues of $55 million are anticipated. Today, Douglas machines are used in nearly every state in the U.S. and in fifteen countries worldwide.

7/7/97

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