



Memorandum

TO: COMMUNITY AND
ECONOMIC DEVELOPMENT
COMMITTEE

FROM: Jeff Ruster, Deputy Director
Office of Economic
Development

SUBJECT: CATALYST PROGRAM

DATE: October 9, 2009

Approved

Date

10/2/09

RECOMMENDATION

Accept the progress report of the investment activities of the Economic Development Catalyst Fund.

BACKGROUND

In January 2007, the City executed an Investment Management Agreement with Pacific Community Management (PCM) to provide investment management services for the City's Economic Development Catalyst Program (EDCP). Over the 10-year term of the Agreement, PCM will recommend, perform due diligence, and facilitate investments in high potential small businesses with: (1) positive cash flow, (2) annual revenues of at least \$3 million, (3) a strong management team in place, and (4) a clear path toward growth and increased profitability. Additionally, PCM's mission supports the identification of small businesses that will provide training, benefits, and profit-sharing opportunities for low- and moderate-income employees.

The City will provide up to \$3 million over the next three years to leverage substantial venture capital investment in private San Jose small businesses. PCM will match every City dollar invested through the EDCP with a minimum of \$5.70 from PCM and other co-investors. In addition to increasing the direct impact of City funds, the EDCP is anticipated to make equity investments that will enhance job creation, expand the local tax base, and facilitate the integration of other programs and services targeted to the small business community.

For the inaugural EDCP investment, the City made a \$350,000 preferred stock investment in Bentek, at a leverage ratio of 5.7:1. Subsequently, the City made a \$502,000 preferred stock investment in Kimomex Markets; the leverage ratio for this investment was 10.8:1. Since these initial investments were made, the City has reviewed and approved various transactions to assist its portfolio companies to address liquidity issues.

ANALYSIS

The past year has been a time of economic hardship for many businesses including the EDCP's two portfolio companies. Both have implemented aggressive cost reductions. During this time, PCM has focused on supporting the City's existing EDCP investments by assisting to establish or restructure debt, recruiting management team members, and upgrading financial and operating reporting capabilities.

COMMUNITY AND ECONOMIC DEVELOPMENT COMMITTEE

Subject: Economic Development Catalyst Program Update

October 9, 2009

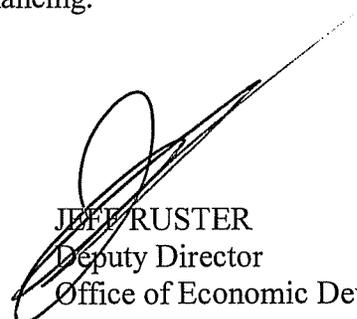
Page 2 of 2

Despite numerous cost restrictions, Bentek was able to develop a product for the rapidly growing solar industry. This product, a solar combiner, is an essential part of industrial and commercial solar arrays. The gross margins on the solar combiner are significantly higher than those generated in Bentek's traditional custom build business, and these solar combiners have been installed in a number of solar arrays. Bentek anticipates a continued sales focus in this area.

In order to identify new investment opportunities for the EDCP, PCM leverages multiple sources, including the City of San Jose and affiliated agencies, business brokers and bankers, small business support organizations, the Hispanic community, and other investor groups. Additionally, PCM provides strategic guidance and business education to a pipeline of potential portfolio companies through its ADVANCE program, offering one-on-one advisory sessions and educational forums with prominent business school professors and corporate leaders.

Over the past year, PCM has reviewed and negotiated several new investments, but none were determined to be a good fit for the EDCP. PCM is now seeing signs of recovery in the market and has refocused its efforts on identifying attractive investment opportunities for the EDCP. PCM has recently updated its databases and rescreened for potential investment candidates. Several high probability targets have emerged, and PCM expects to enter new financing discussions shortly, with possible additional EDCP investments to be made in the fourth quarter of 2009.

PCM is currently structuring a deal with a sporting equipment designer, marketer, and manufacturer located in San Jose, identified through PCM's annual screening of all private companies located in San Jose. Although this company was originally identified as a potential investment candidate last year, negotiations were put on hold when the company decided to forgo outside equity. Since that time, the company has designed a new product that is ready to be launched and that will need growth equity financing.



JEFF RUSTER
Deputy Director
Office of Economic Development

Office of Economic Development

ECONOMIC DEVELOPMENT CATALYST PROGRAM

Presentation to
Community & Economic Development
Committee

October 26, 2009



Economic Development Catalyst Program

- **PROGRAM OBJECTIVES AND DESIGN**

- Support high growth companies
- Leverage City capital contribution
- Generate financial return
- Connect dots with other City programs
- Investment agreement with Pacific Community Management (PCM)

Economic Development Catalyst Program

• **CURRENT EDCP PORTFOLIO COMPANIES**

- **Bentek**

- High-complexity, low-volume contract manufacturing services
- \$350K of preferred stock
- Leveraging of 8.6:1

- **Kimomex**

- Hispanic-themed grocery stores
- \$502K of preferred stock
- Leveraging of 16.8:1

Office of Economic Development

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Economic Development Catalyst Program

- **LOOKING FORWARD**

- Current economic conditions and impact on EDCP investments
- PCM's technical assistance to portfolio companies

- **ANTICIPATED INVESTMENT PIPELINE**

- Annual screening for potential San Jose investments
- Strategic guidance and business education for companies in pipeline
- Other PCM value adds
- Potential new Catalyst investments