CURRENT ISSUES IN MINORITY ENTREPRENEURSHIP

A SCAN ON THE STATE OF MINORITY ENTERPRISE IN THE UNITED STATES

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Rationale for Focus of Minority Entrepreneurship Scan

In the discussions to define the scope of the minority entrepreneurship scan, it was agreed that we would discuss entrepreneurship from a public policy perspective, and, in particular, we would focus on those aspects of entrepreneurship which

- contribute to economic development and community growth,
- create jobs,
- build businesses, and
- lead to wealth creation, not simply for an individual but for a larger community.

We looked at entrepreneurial activity in the mainstream and found that the companies that fulfilled these criteria the best over the last two decades were entrepreneurial companies in the technology sector. Technology companies, ranging from Lotus and Microsoft to eBay and Amazon, have been among the most efficient in building lasting businesses, creating jobs and creating community wealth.

Non technology industries, in such areas as traditional manufacturing and retailing, have had significant companies but their need for high levels of capital and their relatively slower rate of growth puts them on a lower priority when it comes to policymaking.

We also found that, particularly as part of the minority entrepreneurship landscape, mergers and acquisitions, corporate divestitures and roll-ups – while legitimate and significant areas of private equity activity – were more about dealmaking than entrepreneurship. The short-term impact of these activities on jobs and business-building was often harmful to a local economy and to unskilled labor. As a result we felt that start-ups should be the major focus of the entrepreneurial scan.
Based on our observations we suspected that different ethnic groups had different rates of success in raising capital for entrepreneurial businesses. When we looked closer we found that it appeared to be true. The data showed that these differential rates of success appeared to be influenced not only by changing demographics but differential participation in education and in business as well. We felt that only by expanding the discussion to discuss changing demographics and the differential rates of participation in various areas could we get a more complete picture of minority entrepreneurship today.
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INTRODUCTION

Minority enterprise and its growth are critical to the future of the United States. Entrepreneurial businesses, the segment of the economy that is the fastest growing, have the greatest potential for creating jobs and contributing to economic expansion. As the traditional minority groups begin to outnumber the Caucasian population – according to the Census Bureau, minority groups will outnumber the Caucasian population after 2050 – minorities must become more involved in the entrepreneurial process to ensure the future sustainability and growth of the U.S. economy.

The purpose of this report is to contribute to the public dialogue on minority enterprise, and to expand the discussion to include the specific groups that comprise the vast majority of those groups making up the category “minority”: Asian/Pacific Islanders, African Americans, Hispanics and Native Americans. Differences in these groups’ experiences are significant and intriguing, but are too often overlooked or ignored. Opening this discussion should challenge all parties involved in developing policies and programs affecting minority enterprise to further explore current trends, roots of these trends, and new directions for the future.

There are four sections of this report. The first section reviews the origins of minority enterprise programs, other sources of capital today, and the status of minority enterprise by race and origin. The second defines minority enterprise and observes trends in education and employment for each group. The third explores sources of funding as the fuel of minority enterprise, specifically what the roles of government programs, mainstream venture capital, and minority venture capital have been. Finally, the fourth section offers recommendations to accelerate minority enterprise growth across the board.

1 The terms Asian/Pacific Islander, African American, Hispanic and Native American are used throughout the narrative for the purposes of consistency. However, different terms may have been used by the many sources cited.
HISTORY OF MINORITY ENTERPRISE

In 1969, the Minority Enterprise Small Business Investment Company (MESBIC) Act gave rise to the specialized venture capital firms that invest in minority-owned businesses. Since that time, these Specialized Small Business Investment Companies (SSBICs) have provided over $2,250.1 million\(^2\) in capital to 20,403\(^3\) minority-owned businesses. Today, specialized venture funds that target minority-owned businesses and businesses that involve minorities have assets in excess of $5 billion and provide financing to an estimated 200 or so companies each year. Mainstream venture funds, which do not track their investments by race, provide financing to another 50 or so companies operated and owned by minorities.

It is ironic that it required legislation to create an investment program for minority entrepreneurship. Not that the concept of governmental involvement in promoting entrepreneurship was new. Reacting to criticism that the U.S. was falling behind the then-U.S.S.R. in the technology race, especially space race, the Eisenhower Administration proposed small business investment legislation which the Congress enacted into the Small Business Investment Company (SBIC) Act into law in 1958. The new law created private investment companies, termed SBICs, that could borrow up to two dollars of government loans for every dollar in private equity they raised and invested. It also laid the foundation for what has become the venture capital industry of today.

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Creation of MESBICs

Nearly a decade later, amidst the urban unrest devastating America’s inner cities, the Johnson Administration, responding to the Kerner Commission Report, proposed an investment program for minorities, similar to the SBIC program already in existence. Labeled the MESBIC program, the private investment companies formed under the new program were chartered to invest exclusively in businesses owned by minorities and women. For every dollar of private equity that a MESBIC raised, it could receive up to four dollars in government leverage. Not much private equity flowed into the MESBIC program in its early days. Most came from the social responsibility allocation of corporations and from not-for-profit groups who sought to infuse the minority communities with capital. Indeed, the lack of financially-oriented capital may have restricted the initial vision and goals of the MESBIC movement.

For most of its early days, MESBICs invested extensively in media-related businesses, including radio, television and cable television properties. Their strategy wasn’t so much classic venture as it was private equity: the financing of existing businesses in order to achieve economies of scale and create minority ownership. The strategy received a further boost in the late 1970s when the Federal Communications Commission proposed such rules as tax certificates and distress sale procedures to encourage greater diversity of media ownership.

In the mid-1970s, the change in Employee Retirement Income Security Act (ERISA) rules created a new influx of capital into the mainstream venture capital industry. The formation of funds such as Kleiner Perkins Caufield & Byers, the Mayfield Fund, Oak Investment Partners and others that invested almost exclusively in technology gave rise to the first venture-driven bull market that began in the early 1980s. Unfortunately, MESBICs did not participate in this technology funding. However, when the technology markets collapsed in 1983 and venture funds reported a major cyclical collapse in their returns, the MESBICs didn’t escape unscathed.
By the early 1990s, the MESBIC program was clearly in need of overhaul. The Small Business Administration, which was overseeing the industry, had shown little initiative in shaping the program to cope with the changing economy and the entrepreneurial population. One report, authored by Timothy Bates of Wayne State University, argued that small pools of capital, the dearth of professional investment managers, and rigid government supervision all contributed to the problems experienced by minority venture capital firms.

**MESBICs Transformed**

The changes began with public pension fund support, the formation of a fund-of-funds to direct capital exclusively to minority-oriented venture funds and the growing visibility of a number of minority-backed businesses and minority entrepreneurs.

The Michael Milken engineered buyout of Beatrice International’s non-U.S. properties by Reginald Lewis, an African-American lawyer, for $970 million, the initial public offering of Envirotest, an environmental testing company, and the growth of Black Entertainment Television (BET) suggested that minority entrepreneurs could compete in a broader economy. Certainly, the successes recently experienced by Radio One, founded by African-American entrepreneur Kathy Hughes, and Granite Broadcasting, a television station chain operated by former Goldman Sachs banker, Don Cornwell, indicate that minority-owned businesses can compete for mainstream financing and exist in a broader marketplace.

By the mid 1990s, minority venture capital firms had gone through a metamorphosis. They had, for the most part, reduced their dependence on Small Business Administration (SBA) leverage and were aggressively seeking the participation of public pension funds such as New York State Common Retirement Fund, and California Public Employees Retirement System, as well
as leading commercial banks such as The Bank of America, Fleet Bank and others. At the end of the last decade, venture capital funds that financed minority-owned businesses or businesses targeting minorities managed assets in excess of $5 billion.

But for all the growth in capital, most minority venture capital does not flow to high-technology companies – the core of the mainstream venture capital investing – but to media businesses and roll-up of more traditional companies. Businesses backed by minority venture funds still aren’t an integral part of the mainstream technology economy.

Minority venture capital funds, with few exceptions, have been unable to attract venture capitalists with an understanding of and a background in technology. Unlike mainstream venture capital funds that invariably have partners with high-tech academic or high-tech business backgrounds, few minority venture capitalists have any training in technology. They are poorly networked in the investment banking community as well as in the high-tech community. It is significant that some of the most successful minority entrepreneurs have been funded by mainstream venture funds, not by minority venture funds. Those include Jugi Tandon, one of the first minority entrepreneurs to start a computer business, Suhas Patel, one of the founders of Cirrus Logic, Manny Fernandez, who founded Gavilan Computers, David Hwang of Televideo, and David Lee of Qume. In later years, mainstream venture capitalists have gone on to fund even more prominent minorities, such as Umang Gupta of Gupta Corp., and later Keynote Systems, Kanwal Rekhi of Excelan, Desh Deshpande of Sycamore Networks, Sabir Bhatia of Hotmail, and Jerry Yang of Yahoo.

Minority venture funds have shown poor response time in reacting to technology segment changes, and to individual proposals submitted to them. In terms of reacting to changes in technology, minority venture capitalists have been lagging. In the 1980s, while the technology bull market was led by personal computer and
personal computer-based companies, minority venture funds were focusing on media and communications. While a large portion of the late 1980s dollars was going to medical and biomedical deals, minority venture capitalists were noticeably absent in the area. The few minority-owned medical start-ups that emerged were typically self-funded. Similarly, although the first Internet investments were being made in the early 1990s, it wasn’t until the mid-1990s that minority-owned Internet companies such as NetNoir were founded. Ironically, the initial investment in NetNoir came out of America OnLine and its Greenhouse project.

Minority entrepreneurs we have interviewed complain that most minority funds are not aggressive in seeking out deals nor are they sensitive to the needs of their potential portfolio companies. Entrepreneurs, especially in technology businesses, say that there are few partners in minority venture funds that have any real insight into technology, even fewer have any professional technology education. While mainstream funds have often rectified the problem of being shorthanded in technology by recruiting entrepreneurs to join, minority venture funds have not resorted to such a strategy.

**Capital Gap?**

A recent report prepared by the Milken Institute for the Minority Business Development Agency of the Department of Commerce argues that the capital gap that exists for minority-owned enterprises stood at $140 billion in 1992. The argument, while politically popular, requires closer examination.

The assumption is that minorities – as a homogenous entity – are chronically undercapitalized. On closer examination, however, we will see that different groups have different levels of access and rates of success at obtaining capital. While it is self-evident that all small businesses could benefit from better access to capital and at lower prices, it is not clear that entrepreneurial businesses run by minorities are languishing because of the a lack of growth capital.
A look at the 140 publicly traded companies that are operated and owned (at least 10 percent of the stock is owned by minority managers) shows that companies with Asian/Pacific Islander owners and managers dominate the landscape.

<table>
<thead>
<tr>
<th>Race/Ethnic Group</th>
<th>Number</th>
<th>Percentage of All Minority-Owned Firms</th>
<th>Average Market Cap</th>
<th>Collective Market Cap</th>
</tr>
</thead>
<tbody>
<tr>
<td>African American</td>
<td>17</td>
<td>12.14%</td>
<td>$105,882,353</td>
<td>$1,800,000,000</td>
</tr>
<tr>
<td>Hispanic</td>
<td>30</td>
<td>21.43%</td>
<td>$706,666,667</td>
<td>$21,200,000,000</td>
</tr>
<tr>
<td>Asian/Pacific Islander</td>
<td>93</td>
<td>66.43%</td>
<td>$1,602,150,538</td>
<td>$149,000,000,000</td>
</tr>
</tbody>
</table>

Source: The Chapman Company

According to The Chapman Company, a Baltimore, Md. investment bank and research concern, Asian/Pacific Islanders owned and operated companies such as Alliance Semiconductor, Complete Business Solutions Inc., Computer Associates and Sycamore Networks have had little trouble accessing the capital markets. In the last two years, a number of Hispanic-owned companies such as Starmedia – mostly related to Internet products and services – also have gained access to the capital markets. They join Hispanic Broadcasting and Univision, two of the largest media companies operating in Hispanic markets. Radio One and TeleCommunication Systems, Inc. were among the African-American owned and operated companies that went public in 1999 and 2000, joining such companies as Granite Broadcasting.

At least 7 percent of the 1028 companies that went public in the United States in 2000 had an Asian/Pacific Islander at its helm who had a stake in the company.
This is in sharp contrast to the handful of Hispanic-owned and African-American owned companies that went public the same year.

Companies headquartered in Asian and Latin American countries are routinely raising capital on U.S stock exchanges. Companies such as Infosys, ICICI Bank and Satyam – all based in India – and Brazil’s Embraer Aircraft Corp., AsiaInfo Holdings (Beijing), ASAT Holdings Ltd (Hong Kong) are demonstrating that the markets are open to those companies that can demonstrate shareholder value and potential.

What explains the difference in market access?

Among the minority groups, Asian/Pacific Islanders have the largest presence in technology businesses within the United States. Venture capital firms such as Advent International and Walden Ventures and more recently Softbank (now raising $4 billion for Asia-related Web infrastructure companies) say they are extremely comfortable with Asian and Asian-American entrepreneurs and evaluate them alongside the rest of the technology universe.

Entrepreneurially-driven Hispanic businesses have received an increased flow of venture capital in recent years because of their potential to connect U.S. and Latin American markets and the growing economic strength of the Latin and Hispanic American consumer.

African-American businesses – with few footprints in technology – have generally not been the beneficiaries of large amounts of venture capital. However, entrepreneurs with a technology background – American Express’ John Williams, a founder of Biztravel.com and Maurice B. Tose, who founded TeleCommunication Systems, Inc. – have been able to attract equity investors.
Native American businesses also have been visibly absent from the growth economy. But in recent years, the profits from “protected” businesses such as casinos and natural resource exploration are being channeled into new business areas. The work of the not-for-profit First Nations Development Institute in Fredericksburg, Virginia, which currently operates on an annual investment budget of $2 million, has been a key force in financing new businesses in computer services, manufacturing support systems and a variety of information services and systems companies.

**Different Groups, Different Experiences**

While there are few relevant cross-cultural studies of contemporary entrepreneurship, it is clear that different minority groups have different sets of characteristics and resources. A majority of Asian/Pacific Islanders that have qualified for financing are immigrants who have extensive technology experience here. Hispanic entrepreneurs that have been able to secure equity recently have demonstrated unique access to Latin America and to Hispanic markets here and abroad. By contrast, African Americans and Native Americans have not brought similar “competitive advantages” to the financing table. In recent years, the work of Harvard Business School professor Michael Porter on the competitive advantage of Inner Cities has given African American and Hispanics a new edge. But not too many ideas have emerged to exploit this “advantage”.

Further anecdotal and empirical research in this area is needed to guide existing policy and future policy formulation.
DEFINING AND UNDERSTANDING MINORITY ENTERPRISE

Because existing racial and ethnic minorities are projected to become the majority in the U.S. by 2050\(^4\), the growth of minority-owned firms is expected to determine the sustainability of America’s economy in the future. While there is no comprehensive mechanism for tracking start-up activity among minority businesses, the statistics from the Minority Business Development Agency (MBDA) shed light on this sector.

The MBDA estimates that in 1997, there were 3.25 million minority-owned firms with total sales of $495 billion. The number of minority firms grew at a rate of 17 percent, six times the rate of U.S. firms in general, and sales increased by 34 percent, twice that of all firms. These numbers appear to overstate the actual performance of these groups because the low base numbers.

However, minority-owned firms are still underrepresented in the economy in comparison to their overall percentage of the population, and some groups are disproportionately represented within the total number of minority businesses. For example, in 1995, African Americans, with 13 percent of the population, owned only 6.5 percent of all minority businesses, while Asian/Pacific Islanders, at 4 percent of the population, owned 32.9 percent of minority businesses.

There is also significant disproportionate-ness in the financing of minority business by SBA programs. For the period October 1999 to September 2000, African-American owned businesses represented only 1.44 percent (by amount) of such financings and Hispanic-owned business 0.55 percent. However Asian/Pacific Islander-owned businesses represented 2.02 percent. Native American owned businesses represented 0.04 percent.\(^5\)


These ratios vary little whether one examines so-called regular SBICs or Specialized SBICs. Businesses owned by African Americans accounted for 35.56 percent of all financings to minority-owned businesses, whereas the percentage of such financings by SBICs was 33.33 percent and by SSBIC’s 41.88 percent. Hispanic-owned firms accounted for 13.58 percent of all financings to minority owned firms, 14.19 percent of those financings by SBIC’s and 12.55 percent of those financings by SSBIC’s. Firms owned by Asian/Pacific Islanders accounted for 49.88 percent of all financings to minority-owned firms, 51.16 percent of those financings by SBIC’s and 45.45 percent of those financings by SSBIC’s. The percentages for Native American-owned firms were 0.99 percent of all financings to minority owned firms, 1.32 percent of those financings by SBICs and 0.12 percent of those financings by SSBICs.

<table>
<thead>
<tr>
<th>Majority Ownership</th>
<th>Overall Financings</th>
<th>SBICs</th>
<th>SSBICs</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Percentage of All Financings</td>
<td>Percentage of All Financings to Minority Owned Firms</td>
<td>Percentage of All Financings by SBICs to Minority Owned Firms</td>
</tr>
<tr>
<td>African American</td>
<td>1.44%</td>
<td>35.56%</td>
<td>1.01%</td>
</tr>
<tr>
<td>Hispanic</td>
<td>0.55%</td>
<td>13.58%</td>
<td>0.43%</td>
</tr>
<tr>
<td>Asian/Pacific Islander</td>
<td>2.02%</td>
<td>49.88%</td>
<td>1.55%</td>
</tr>
<tr>
<td>Native American</td>
<td>0.04%</td>
<td>0.99%</td>
<td>0.04%</td>
</tr>
<tr>
<td>Overall</td>
<td>4.05%</td>
<td>100.01%</td>
<td>3.03%</td>
</tr>
</tbody>
</table>

Source: Small Business Administration, SBIC Program Statistical Package, Financing to Small Businesses, Recorded For Fiscal Year 2000 Only, Table 11
The disproportionate percentage of SBIC financings may be due unequal rates of participation in technology-related education and the technology-related workforce, and differing entrepreneurial experiences within each minority group.

**Minority Participation in Technology Education**

If technology is the driving force behind the most successful business enterprises in this country, the pool of prospective minority entrepreneurs in this area is largely limited by the number of African-American, Hispanic and Native American individuals who pursue higher education in science and engineering. Additionally, there is a correlation between each minority group’s representation in higher education and the work force, and the numbers of successful entrepreneurs.

**Science and Engineering Bachelor Degrees, by Race and Hispanic Origin**

Research by the National Science Foundation shows that for the most part, African Americans, Hispanics and Native Americans are underrepresented, but that Asian/Pacific Islanders are over-represented in science and engineering bachelor’s, master’s and doctorate programs. In 1995, the population of 18 to 30-year olds of U.S. residents was Asian/Pacific Islander 4 percent, African American 14 percent, Hispanic 13 percent, and Native American 0.8 percent. However, a review of the number of science and engineering bachelor’s degrees conferred in 1996 shows that Asian/Pacific Islanders earned 7.93 percent these degrees, while African Americans earned 7.43 percent, Hispanics 6.08 percent, and Native Americans 0.58 percent.

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### Science and Engineering Bachelor's Degrees

Conferred to U.S. Citizens or Permanent Residents in 1996, By Race and Hispanic Origin

<table>
<thead>
<tr>
<th></th>
<th>Asian/Pacific Islander</th>
<th>African American</th>
<th>Hispanic</th>
<th>Native American</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Number</td>
<td>Percent</td>
<td>Number</td>
<td>Percent</td>
</tr>
<tr>
<td>U.S. Population 18-30 (1995)</td>
<td>63,117</td>
<td>5.53%</td>
<td>89,554</td>
<td>7.84%</td>
</tr>
<tr>
<td>All Degrees (any field)</td>
<td>31,031</td>
<td>7.93%</td>
<td>29,055</td>
<td>7.43%</td>
</tr>
<tr>
<td>Natural sciences</td>
<td>9,829</td>
<td>10.22%</td>
<td>5,274</td>
<td>5.48%</td>
</tr>
<tr>
<td>Math and computer sciences</td>
<td>3,383</td>
<td>9.70%</td>
<td>3,396</td>
<td>9.74%</td>
</tr>
<tr>
<td>Engineering</td>
<td>6,799</td>
<td>11.66%</td>
<td>3,000</td>
<td>5.15%</td>
</tr>
</tbody>
</table>


The disparity between each group’s representation in the 18 to 30 year-old population and the percentage of science and engineering bachelor’s degrees earned in 1996 is greater in fields more closely related to high technology. In the area of mathematics and computer science, Asian/Pacific Islanders earned 9.70 percent of bachelor’s degrees, African Americans earned 9.74 percent, Hispanics earned 5.35 percent, and Native Americans earned .41 percent. In engineering, Asian/Pacific Islanders earned 11.66 percent of degrees, African Americans earned 5.15 percent, Hispanics earned 6.40 percent, and Native Americans earned 0.42 percent. Asian/Pacific Islanders and African Americans favored mathematics and computer science, and Asian/Pacific Islanders and Hispanics favored engineering.\(^8\)

Engineering technology, which is not considered a science and engineering degree, was slightly favored by all underrepresented minorities and disfavored by Asian/Pacific Islanders. Of the bachelor's degrees in engineering technology

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conferred, Asian/Pacific Islanders received 4.79 percent, African Americans 8.99 percent, Hispanics 6.49 percent, and Native Americans 0.74 percent.\(^9\)

**Longitudinal Increases in Science and Engineering Bachelor's Degrees among Minorities, from 1977 to 1996**

These figures must be considered in the context of a longitudinal increase in the number and percentage of minorities pursuing higher education, and science and engineering in particular. A National Science Foundation analysis of Census Bureau, Department of Education, and its own data showed that a higher percentage of the 24 year-old general and minority population had bachelor degrees in 1996 than 1980. For the total 24 year-old population, the percentage increased to 32.1 from 22.2; Asian/Pacific Islanders increased to 39.2 from 29.5, African Americans increased to 17.7 from 11.2, Hispanics increased to 14.2 from 10.5, and Native Americans increased to 20.6 from 12.1.\(^{10}\)

A comparison of bachelor degrees conferred in 1977 and 1996 also shows that an increasing number of U.S. citizens and permanent residents earning bachelor's degrees, with minorities earning a greater percentage of the science and engineering degrees than in the past. In 1977, a total of 910,835 bachelor’s degrees were conferred, and in 1996, a total of 1,142,028 were, with a decreasing percentage (36.16 percent in 1977 and 34.24 percent in 1996) in science and engineering.\(^{11}\)

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### Percentage of Science and Engineering Bachelor’s Degrees Conferred to U.S. Citizens or Permanent Residents in 1996, by Race and Hispanic Origin

<table>
<thead>
<tr>
<th></th>
<th>Asian/Pacific Islander</th>
<th>African American</th>
<th>Hispanic</th>
<th>Native American</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Science and Engineering</td>
<td>1.88%</td>
<td>7.93%</td>
<td>5.94%</td>
<td>7.43%</td>
</tr>
<tr>
<td>Natural sciences</td>
<td>2.01%</td>
<td>10.22%</td>
<td>3.55%</td>
<td>5.48%</td>
</tr>
<tr>
<td>Math and computer sciences</td>
<td>2.38%</td>
<td>9.70%</td>
<td>5.33%</td>
<td>9.74%</td>
</tr>
<tr>
<td>Engineering</td>
<td>2.63%</td>
<td>11.66%</td>
<td>3.00%</td>
<td>5.15%</td>
</tr>
</tbody>
</table>

Source: National Science Foundation, "Science & Engineering Indicators – 2000"

All minority groups experienced significant gains in share of science and engineering bachelor’s degrees during the period 1977 to 1996. Asian/Pacific Islanders experienced the largest gain, increasing to 9.70 percent in 1996 from 2.38 percent of mathematics and computer science degrees in 1977, to 11.66 percent and from 2.36 percent of engineering degrees. African Americans increased their share of these degrees by more than 50 percent. African Americans earned 5.33 percent of mathematics and computer science degrees in 1977 and 9.74 percent in 1996, and 3.0 percent and 5.15 percent of engineering degrees. Hispanics more than doubled their share of mathematics and computer science, and engineering degrees, earning 5.35 percent and 6.40 percent of these degrees by 1996. Native Americans also doubled their share of mathematics and computer science degrees, and increased their share of engineering degrees by nearly 50 percent.

### Master’s and Doctorate Degrees, by Race and Origin

This trend of under- and over-representation by race and origin becomes more pronounced when one examines the percentage of science and engineering master’s and doctorate degrees conferred to U.S. citizens and permanent residents during 1996. After obtaining a bachelor’s degree, African Americans and Hispanics tend to end high technology-related education, while Asian/Pacific Islanders have a higher tendency to continue pursuing higher education. The more advanced the degree, the lower the percentage of degrees conferred to
African Americans and Hispanics. For Native Americans, the percentage decreases for master’s degrees, but increases slightly for doctorate degrees. Meanwhile, the percentage of degrees conferred to Asian/Pacific Islanders increases for each field, with the exception of natural sciences which decreases for master’s degrees but increases for doctorates.\textsuperscript{12}

<table>
<thead>
<tr>
<th>Field and race/ethnicity</th>
<th>Bachelor’s Degrees</th>
<th>Master’s Degrees</th>
<th>Doctorate Degrees</th>
</tr>
</thead>
<tbody>
<tr>
<td>Asian/Pacific Islander</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Science and engineering:</td>
<td>31,031</td>
<td>5,942</td>
<td>3,091</td>
</tr>
<tr>
<td>Natural sciences</td>
<td>9,829</td>
<td>933</td>
<td>1,550</td>
</tr>
<tr>
<td>Math and computer sciences</td>
<td>3,383</td>
<td>1,472</td>
<td>251</td>
</tr>
<tr>
<td>Engineering</td>
<td>6,799</td>
<td>2,621</td>
<td>895</td>
</tr>
<tr>
<td>African American</td>
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<tr>
<td>Science and engineering:</td>
<td>29,055</td>
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<tr>
<td>Natural sciences</td>
<td>5,274</td>
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<td>187</td>
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<tr>
<td>Math and computer sciences</td>
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<td>530</td>
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<tr>
<td>Engineering</td>
<td>3,000</td>
<td>674</td>
<td>74</td>
</tr>
<tr>
<td>Hispanic</td>
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<td></td>
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<tr>
<td>Science and engineering:</td>
<td>23,791</td>
<td>2,730</td>
<td>623</td>
</tr>
<tr>
<td>Natural sciences</td>
<td>4,899</td>
<td>413</td>
<td>229</td>
</tr>
<tr>
<td>Math and computer sciences</td>
<td>1,865</td>
<td>264</td>
<td>26</td>
</tr>
<tr>
<td>Engineering</td>
<td>3,731</td>
<td>748</td>
<td>98</td>
</tr>
<tr>
<td>Native American</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Science and engineering:</td>
<td>2,268</td>
<td>304</td>
<td>96</td>
</tr>
<tr>
<td>Natural sciences</td>
<td>559</td>
<td>41</td>
<td>34</td>
</tr>
<tr>
<td>Math and computer sciences</td>
<td>142</td>
<td>30</td>
<td>5</td>
</tr>
<tr>
<td>Engineering</td>
<td>243</td>
<td>56</td>
<td>14</td>
</tr>
</tbody>
</table>

Source: National Science Foundation, “Science & Engineering Indicators – 2000”

Again, these differences in advanced degrees are most pronounced in the high technology-related fields. In 1996, the percentage of Asian/Pacific Islanders who were conferred mathematics and computer science bachelor’s, master’s, and doctorate degrees steadily climbed from 9.70 percent to 15.81 percent to 21.66 percent. Notably, African Americans accounted for more mathematics and computer science bachelor’s degrees during that year, 9.74 percent. But master’s degrees dropped to 6.69 percent, and doctorate degrees dropped most dramatically to 1.73 percent. Mathematics and computer science advanced degrees dropped most significantly for Hispanics at the master’s degree level, starting with 5.35 percent of mathematics and computer science bachelor’s degrees, then declining by more than half to 2.34 of master’s degrees, then 2.24 percent of doctorates.13

For engineering, during 1996, Asian/Pacific Islanders earned 11.66 percent of bachelor’s degrees but 26.46 percent of doctorates. The percentages dropped for African Americans, from 5.15 percent of bachelor’s, to 3.59 percent of master’s degrees, and 2.19 percent of doctorates. Hispanics started with 6.40 percent of bachelor’s, declined to 3.99 percent of master’s, then to 2.90 percent of doctorates.14

Comparing the frequency that various minority groups obtain degrees in specific science and engineering fields to their Caucasian counterparts offers another perspective. A study by the Department of Education of degrees conferred in 1996 shows that Asian/Pacific Islanders are 3.47 times as likely as Caucasians to earn a master’s degree in computer science and engineering. African Americans were only 0.69 times as likely, Hispanics were 0.98 as likely, and Native Americans were 0.75 as likely. Each group, with the exception of


Hispanics, was more likely to study computer and information sciences and slightly less likely to study engineering and engineering technologies.\textsuperscript{15}

| Field Concentration Ratio of Master’s Degrees Conferred, by Field of Study, 1996 |
|-----------------------------------------------|----------------|----------------|----------------|----------------|----------------|
|                                               | Caucasian | Asian/ Pacific Islander | African American | Hispanic | Native American |
| Computer Sciences and Engineering             | 1.00      | 3.47                      | .69               | .98       | .75             |
| Computer and information sciences             | 1.00      | 4.94                      | 1.07              | .84       | .95             |
| Engineering and engineering technologies      | 1.00      | 3.04                      | .59               | 1.02      | .69             |


The Impact of Pre-College Education

The roots of the disparity in the numbers of underrepresented minorities pursuing higher education and careers in science and technology lay partly in pre-college education. African American, Hispanic, and Native American students attend schools with fewer resources, and are less likely to take advanced courses in science and mathematics. Meanwhile, Asian/Pacific Islander students were more likely to take advanced courses.

A study by the National Science Foundation reported that a high percentage of African Americans (32 percent) and Hispanic students (25 percent) attend central city schools, which tend to have fewer resources to offer higher level math and science courses.\textsuperscript{16} From 1977 to 1996, a much higher percentage of Caucasian students ages 9, 13 and 17 scored at or above the National Assessment of Educational Progress (NEAP) benchmark than their African American and Hispanic counterparts. For example, in 1996, 86 percent of 13


year-old Caucasian students, 54 percent of African American students, and 58 percent of Hispanic students scored at the 250 NEAP benchmark.\(^\text{17}\)

African-American, Hispanic and Native American minority students are also less likely than their Asian/Pacific Islander and Caucasian counterparts to take Advanced Placement courses. In 1996, these students were 25 percent of the population, but were only 5 to 10 percent of Advanced Placement exam test-takers.\(^\text{18}\)

A review of the percentage of high school graduates who took Advanced Placement and honors mathematics and science courses in 1994 shows that Asian/Pacific Islander students were more likely than their Caucasian, African American, Hispanic and Native American counterparts to take these courses.\(^\text{19}\)

<table>
<thead>
<tr>
<th>Courses</th>
<th>Caucasian</th>
<th>African American</th>
<th>Hispanic</th>
<th>Asian/Pacific Islander</th>
<th>Native American</th>
</tr>
</thead>
<tbody>
<tr>
<td>AP Calculus</td>
<td>7.3%</td>
<td>2.0%</td>
<td>4.6%</td>
<td>21.0%</td>
<td>2.2%</td>
</tr>
<tr>
<td>AP/Honors Biology</td>
<td>4.6%</td>
<td>2.7%</td>
<td>3.3%</td>
<td>8.3%</td>
<td>1.7%</td>
</tr>
<tr>
<td>AP/Honors Chemistry</td>
<td>4.3%</td>
<td>2.1%</td>
<td>2.5%</td>
<td>7.7%</td>
<td>0.6%</td>
</tr>
<tr>
<td>AP/Honors Physics</td>
<td>2.5%</td>
<td>1.4%</td>
<td>1.8%</td>
<td>6.0%</td>
<td>0.3%</td>
</tr>
</tbody>
</table>


Representation in the Science and Engineering Workforce, by Race and Origin

This trend of African American, Hispanic and Native American under-representation, and Asian/Pacific Islander over-representation, in secondary education and higher education continues into the science, engineering, and technology workforce.

In 1997, minority representation in the science, engineering and technology workforce was Asian/Pacific Islander 11.2 percent, African American 3.2 percent, Hispanic 3 percent, and Native American 0.3 percent. More specifically, representation in the computer science workforce was African Americans 4.3 percent, Asian/Pacific Islanders were 12.2 percent, Hispanics were 2.6 percent, and Native Americans were 0.2 percent. And for engineering, representation was African Americans 2.6 percent, Asian/Pacific Islanders were 10.9 percent, Hispanics were 3.5 percent and Native Americans were 0.3 percent.\(^\text{20}\)

Additionally, a significant number of foreign science and engineering graduate students who earn degrees in the United States remain here. Approximately 53 percent of foreign students who earned science and engineering doctoral degrees in 1992 and 1993 were working in the United States in 1997. These rates were particularly high for students from China (97 percent) and India (90 percent).\textsuperscript{21}

**Employment as a Source of Entrepreneurial Experience**

It is widely assumed that a significant percentage of entrepreneurs starting technology companies have had experience as managers or engineers at another technology company. Although we are not aware of any statistical studies of this phenomenon, the anecdotal evidence appears to be overwhelming.

An analysis of the available data from the Equal Employment Opportunity Commission with respect to the participation rate for members of minority groups in managerial, professional and technical positions at technology firms indicates that African Americans and Hispanics lag behind in this crucial opportunity for relevant experience. Asian/Pacific Islander show no such deficiency. Indeed, the statistics for investments by SBICs mirrors these statistics and show that a disproportionate percentage of investment in minority owned companies is in Asian/Pacific Islander owned companies, even when the investments of SSBICs are considered separately.

As projected by the United States Census Bureau, African American represented 12.91 percent of the overall population in 2000, with Hispanics representing 10.37 percent, Asian/Pacific Islanders representing 4.09 percent and Native Americans/Alaskan Natives representing 0.87 percent. However, the participation rates are drastically different if you examine the numbers of managers, professionals and technicians in those industries identified by the SBA as “high technology.” Although African Americans represent 8.01 percent of the overall employees of those companies, they represent only 4.96 percent of the managers, professionals and technicians. Similarly, Hispanics represent 6.49 percent of the overall employees of those companies but only 3.79 percent of the managers, professionals and technicians. Conversely, Asian/Pacific Islanders represent 8.46 percent of the overall employees of those companies and 9.63 percent of the managers, professionals and technicians. Native Americans/Alaskan Natives represent 0.55 percent of the overall employees of those companies and 0.42 percent of the managers, professionals and technicians.

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22 MBDA: The Emerging Minority Marketplace, Table 1, Projections and Percent Distribution of the Population by Race and Hispanic Origin: 1995 to 2050
### Minority Participation in High Technology Firms

<table>
<thead>
<tr>
<th></th>
<th>Percentage of Overall Population</th>
<th>Percentage of All Employees</th>
<th>Percentage of Managers, Professional and Technicians</th>
</tr>
</thead>
<tbody>
<tr>
<td>African American</td>
<td>12.91%</td>
<td>8.01%</td>
<td>4.96%</td>
</tr>
<tr>
<td>Hispanic</td>
<td>10.37%</td>
<td>6.49%</td>
<td>3.79%</td>
</tr>
<tr>
<td>Asian/Pacific Islander</td>
<td>4.09%</td>
<td>8.46%</td>
<td>9.63%</td>
</tr>
<tr>
<td>Native American</td>
<td>0.87%</td>
<td>0.55%</td>
<td>0.42%</td>
</tr>
</tbody>
</table>


A recent class action suit brought by certain African American employees against Microsoft provides additional information on minority employment characteristics at large high-tech businesses such as Microsoft. In 1998, the company employed 18,387 people, of whom 82 percent were Caucasian and only 2.6 percent were African American. Furthermore, there was a disproportionately low number of African-American managers when compared to professional staff. Eighty percent of professionals and 87 percent of managers were Caucasian, while 2.7 percent of professionals only 1.21 percent of managers were African American.

**Differences in Entrepreneurship by Race and Origin**

Differences in the rates of successful entrepreneurs by race and origin may also be explained by beneficial or detrimental experiences more commonly shared by specific groups. A study conducted by researchers at the University of North Carolina found that Hispanic entrepreneurs in the Southeastern United States, like other entrepreneurs, were more likely to take risks, and had a need for control and achievement. They also had a family history of entrepreneurship, were heavily involved in networking, and had the ability to communicate in English. They also tended to be community leaders.  

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23 Galbraith, Craig S., and Donald R. Latham and Jacqueline Benitez Galbraith, “Entrepreneurship in the Hispanic Community of Southeastern United States”, University of North Carolina.
Recent articles suggest that some of these and other factors may also influence success among African American entrepreneurs. Further research comparing the impact of specific factors on entrepreneurs across race and origin would be useful in developing policy and programs to address the disproportionate rates of participation.

Some areas to be explored might include historic and perceived access to capital; exposure to capital; and involvement in networking, which are discussed below. Another factor is the relationship between immigration and entrepreneurship. It is significant that a majority of Asian/Pacific Islanders funded by mainstream venture capitalists are recent immigrants.

A historic lack of access to capital from banks and private investors, and possibly bias, continue to have an impact on African Americans today. It is estimated that African Americans received less than 0.25 percent of the $46.5 billion in private equity invested in 1999. Some African American entrepreneurs feel that they are subjected to a higher threshold for raising capital than Caucasians and Asian/Pacific Islanders.\(^\text{24}\) By contrast, many Hispanics feel that there has been an improvement in their access to bank loans over the past 20 years.\(^\text{25}\) Bias, intentional or not, does affect capital access. Additionally, perceived bias may also impact on aggressiveness in seeking and success in obtaining capital.

The percentage of individuals seeking further education and careers in high technology may be influenced by exposure to technology and technology use. When it comes to Internet usage by households, which increases cyber-literacy,


African Americans have the lowest percentage and Asian/Pacific Islanders have the highest.\textsuperscript{26} Likewise, Hispanics did not study fields such as engineering in the past because they felt that they would not be accepted within the industry and few others in their community pursued such careers.\textsuperscript{27}

Involvement in mainstream networking along industry lines may also have an impact on an entrepreneur’s success. The Indus Entrepreneurs (TIE) and the Washington High Tech Council have both emerged as powerful networks of Asian/Pacific Islander entrepreneurs. Their ranks consist of some extremely successful CEOs who in turn have become angel investors in new minority ventures. These entrepreneurial networks provide valuable guidance and capital, they also open the doors to many companies.

While African American technology and entrepreneurial networking groups have sprouted on both coasts and in the Midwest, many of the people of color are not involved in networking outside of these groups. These networking groups include the Network, Minority Internet and Technology Professionals (MITP), Chicago InterNetworking, Network of African American Technology Entrepreneurs List (NATELi), and Bay Area InterNetwork.\textsuperscript{28} In the Hispanic community, there is National Internet Community of Hispanic Entrepreneurs (NICHE-Net). However, some also feel that more Hispanics would be successful if they became involved in mainstream networks for their industries.\textsuperscript{29}

FUNDING FOR MINORITY ENTERPRISES

If one distinguishes between programs aimed at growth or entrepreneurial companies anticipating or attaining rapid growth, entrepreneurial financing programs such as the Small Business Investment Companies (SBIC) program and the Small Business Innovation Research (SBIR) program have had limited impact on the overall growth of minority-owned entrepreneurial companies.

Most enterprises are funded by a combination of equity, debt, sales and miscellaneous sources of capital, such as grants. The combination varies with the growth characteristics of the business and the ability of the capital to grow exponentially. High growth business tends to require large infusions of capital at an early stage where there are few assets – fixed or movable – that can be collateralized. Slower growing businesses have to build their asset base before they can attract capital, which is mostly in the form of debt. Most businesses rely on the profit from sales to fund growth.

Minority enterprises are no different. Their demographics limit their ability to borrow. And there are relatively few companies that fit into the venture capital mold. As a result, large numbers of minority-owned businesses have relied on selling to corporations as a major source of revenue and growth. According to the National Minority Supplier Development Council (MSDC), a New York-based group that certifies minority-owned businesses, minority business enterprises (MBEs) in 2000 sold an estimated $50 billion of goods and services to corporations doing business in the United States.

According to the NMSDC, purchasing activity by corporations from minority businesses has steadily climbed from $86 million in 1972 to $50 billion in 2000.
Nevertheless, few of these companies that sell to corporations have the growth characteristics that will enable them to turn to equity markets to finance their growth. Some of the larger companies that sell to corporations – Louisville’s Active Transportation, Detroit’s Bing Steel – could possibly be candidates for a public stock sale but they need a corporate makeover to qualify. Most of the others are too small to be publicly-owned and traded companies.

Several years ago, a number of corporations had suggested to their suppliers, especially in industry segments where there was a preponderance of small players, that they might consider consolidation or partnering. But the absence of additional corporate interest or economic consequences meant that such ideas were stillborn.

Significantly, a financial infrastructure has evolved to facilitate commerce between minority-owned businesses and their corporate customers. The Business Consortium Fund, a New York financial institution affiliated with the
NMSDC, will finance purchase orders that corporate customers give to their MBEs. In 16 years of its existence, BCF has provided $115.9 million in loans to MBEs. Unfortunately, the BCF serves a very small portion of the MBE universe and it is seen to be extremely slow in responding to its clients. Moreover, its rates and transaction fees, while somewhat lower than those charged by mainstream asset-based lenders can still be quite onerous for small MBEs.

Corporations themselves also have helped finance the operations of their minority suppliers. Ford Motor Co., through its Dearborn Capital SSBIC, has provided a significant amount of capital to MBEs, but has limited its involvement to those companies that do business with the automaker.

Corporate SSBICs such as Dearborn Capital and institutions such as the BCF could be more effective in the markets they serve. Unfortunately, these organizations suffer from a lack of experienced financing professionals as well as limited operating capital, factors that have hurt their ability to play a larger and wider role.

Although the number of corporate dollars directed at minority-owned businesses continues to grow, they are a decreasing proportion of total corporate expenditures. It is believed that corporate America – except in some very select areas – has not assimilated minority-produced goods and services into their “critical” goods and services area. Moreover, there is also the fear that the push towards electronic marketplaces such as Covisint – the procurement portal being jointly developed by Ford, General Motors and Chrysler-Daimler – will reduce minority business access to corporate customers. Most minority businesses aren’t geared to efficiently participate in electronics selling. Moreover, there is a belief that the competition on these purchasing portals will be on price, ignoring some of the key advantages that minority goods and services bring to the marketplace.
Government Programs Aimed at Small Business

The major funding programs for small businesses fall under the auspices of the Small Business Administration. And although the SBA has announced a number of specialized programs aimed at start-up and or minority business, it is doubtful that any of these programs have had, or will have, a major impact on the advancement of businesses owned by minority entrepreneurs.

A number of states and cities also have financing programs aimed at smaller businesses. But these programs have generally proved ineffective as sources of equity capital for small businesses, including MBEs.

The initial government programs directed at minorities were aimed specifically at helping African Americans. Over the next two decades, these programs began to address other minorities as well. But the perception that these programs are primarily African American in scope continues today. Indeed, African-American businesses are the largest group of businesses on certified MBE rosters, followed by Hispanics and Asian/Pacific Islanders.

Overview of SBA Programs

The principal loan program of the SBA is the 7(a) Loan Guaranty Program. The basic parameters of the 7(a) program are (a) that the borrower meets the SBA’s lending criteria, (b) a lender certify that it cannot provide funding on reasonable terms except with an SBA guaranty, and (c) the SBA guarantee is limited to 80 percent on loans up to $100,000 and 75 percent on loans greater than $100,000. In most cases, the maximum guaranty is $750,000 (75 percent of $1 million).

The SBA has recently announced a loan program it calls “CommunityExpress,” supposedly targeted to small businesses in geographic areas covered by the MBDA’s “New Markets” initiative with the purpose of helping small businesses
start, build or grow. These companies have sales less than $2 million per year
and are located in areas in which the poverty rate is 20 percent or more, within a
metropolitan area and in which 50 percent or more of the households in that tract
or division have an income below 60 percent of the area median gross income,
outside a metropolitan area in which the median household income does not
exceed 80 percent of the statewide median household income, within a
HUBZone, within an Urban Empowerment Zone or Urban Enterprise Community
or within an Rural Empowerment Zone or Rural Enterprise Community. However,
this program is limited to a maximum loan of $250,000 with a guarantee limit of
50 percent. (This program is similar to the “SBAExpress” program which has a
$150,000 loan limit and a 50 percent guarantee restriction.)

However, each of these programs is a loan program that requires immediate
positive cash flow to fund the repayment of the loan.

The SBA does have a group of programs designed to assist minority
entrepreneurs compete for Federal contracts, principally the 8(a) Business
Development Program and the Small Disadvantaged Business Certification
Program. In conjunction with these programs it provides management and
technical aid to eligible individuals and small business clients under the 7(i)
Management and Technical Assistance Program. The SBA also has established
an 8(a) mentoring program.

The primary SBA equity program is the Small Business Investment Company
(“SBIC”) program, which now consists of two types of SBICs: the original, or
“regular” SBICs and Specialized Small Business Investment Companies
(“SSBICs”). As noted above, the SSBICs were specifically targeted toward the
needs of entrepreneurs who have been denied the opportunity to own and
operate a business because of social or economic disadvantage. However, the
Small Business Program Improvement Act of 1996 repealed Section 301(d) and,
accordingly, no new SSBIC licenses are being issued but existing 301(d) licensees were “grandfathered” and still in operation.

Although the “leverage” provided by the SBA does increase the pool of available capital, the need to service the debt generated as a consequence of this leverage immediately means that an equity only portfolio is simply not feasible. Indeed, the statistics for financings for the period October 1999 through September 2000 show that a full 57.62 percent of such financings were either straight debt or equity with a debt component.\footnote{“SBIC Program Statistical Package January 2001.” Small Business Administration. 7 February 2001. Small Business Administration. <http://www.sba.gov/INV/stat/2001.html>.
}

**Programs at the Local Level**

States and localities also have “venture capital” programs. However, the lack of any viable exit strategies has caused many of these programs to see their funding dwindle and the programs essentially become limited grant programs rather than equity programs based on the prospect of realizing a return on the equity invested.

The State of Minnesota, for example, has had one of the more expanded programs aimed at financing small businesses. Operated by the Minnesota Investment Network Corporation, the program consists of a $7 million equity fund, the majority of which was already invested in small Minnesota companies by 1999. But the attempt to expand the capital pool of the fund – through capital from the state or from donations – has had limited success.

In terms of state programs, Minnesota’s is one of the more successful. But its scale of investment – less than $1 million – and the small size of its potential portfolio of companies has prevented any substantive recouping of its investment capital and the expansion of the fund.
Other Programs

Other programs have been created by quasi-public entities. For example, the New York City Partnership has created an entity, the New York City Investment Fund, which, according to the organization, "provides funding for projects that stimulate business development, job creation and economic growth in the city and its neighborhoods." However, the funding includes both debt and equity investments and is not limited to for-profit entities, nor is it specifically targeted to minority owned businesses.

Other programs seek to facilitate investment in minority businesses. For example, on January 24, 2001, with great fanfare, AOL Time Warner and the Rev. Jesse Jackson announced the establishment of a program intended to increase opportunities for minority business owners by bringing them together with investors. Called i-DealFlow, the program will include a training program for minority entrepreneurs to hone business plans scheduled this fall to be followed approximately a month later by a venture capital fair.

Mainstream Venture Capital Funding

While we know of no statistics on the dollars flowing from mainstream venture capital firms to minority entrepreneurs, the amounts are significant. A review of several major venture capital firms reveals many such minority-owned businesses.

Starting in the 1980s, with companies such as Tandon Computers and Gupta Corp., venture capitalists have gone on to finance such companies as HotMail, Sycamore Networks, Microstrategy, ShopNow (Network Commerce), and Yahoo, all of which have had significant minority ownership.
Were venture capitalists specifically looking for minority-owned businesses? No. They were looking at companies and ideas that offered returns in keeping with their expectations.

Having minorities as partners in mainstream venture funds also has helped. Kleiner Perkins’ partner Vinod Khosla (a Stanford MBA and India-born) has been a key figure in getting Kleiner Perkins to finance businesses founded and operated by Indians. Mayfield partners Kevin Chang and Yogen Dalal have been instrumental in bringing minority deals to the Palo Alto fund. Other mainstream funds where minority partners have opened the doors to investments in minority-owned businesses include Walden Ventures, Polaris Venture Partners, and Venrock.

**Minority Venture Funds**

Minority funds on the whole, have not participated in the early stages of technological change. Most lack the personnel and resources to identify new technology segments and to support investments in them.

Minority businesses in new technology areas are more likely to need managerial and infrastructure support than their mainstream counterparts. Many of them need help to fill out their management and scientific teams. Unfortunately, minority venture capital firms simply do not have the resources to help fledgling ideas take shape. Minority venture funds continue to be staffed by investors with a financial background – and often little or no technology experience. So when start-ups with minorities at the helm need technology help, these minority venture funds are often in no position to be helpful.

What has also become apparent is that technology companies need increasingly large amounts of capital to be significant players in their markets. The cost of sustaining a business to profitability is much more than it was twenty years ago,
and small venture capital firms, especially minority firms, do not have the capacity to participate effectively and for the long haul.

The few minority venture funds that are large enough to make sizeable investments in companies often lack the infrastructure to provide the broad range of services these companies now need.

In addition, another aspect of the problem is that there is a shortage of deals rather than capital. One role for minority venture funds might be to create a climate where there is more qualified minority deals, providing training to companies by serving as an incubator.

One model to look at might be that of eFiltro Co., a Coral Gables, FL outfit that labels itself as “the premier facilitator for new ventures in the Americas.” The success of eFiltro depends on the team that runs it – a group of technologically proficient Hispanics – and the business and corporate network it has developed. What also helps is its realistic approach to making the venture work.

eFiltro’s goal is to provide a fast and efficient platform for entrepreneurs to obtain funds and for risk capital and enabling companies to select promising ventures. Through its New Idea center, a Web-based database and filter mechanism, business plans are analyzed using a methodology provided to eFiltro by McKinsey & Co. Entrepreneurs submit their business plan to only one source and receive valuable feedback. Capital providers then select concepts that are highly rated and meet their investment preferences.

eFiltro says it has developed key strategic alliances to give it a marketing advantage to obtain deal flow. It has established agreements with over sixty firms to enable it to attract new venture ideas. It has been working with the major Internet portals to reach the general population and the entrepreneurially minded. It also has relationships with universities to host their business plan competitions.
and utilize their students and professors as a variable skilled workforce. It also has agreements with the First Tuesday organization in Miami and Latin America to co-sponsor matchmaking events.

“Our firm has a solid business model that obtains operational profitability, without counting on equity gains, through variable cost structure and multiple revenue streams. We expect positive cash flow within one year, break-even return within two years, and realization of significant equity gains after three years. Our greatest financial strength is the depth and variety of our operation income sources: matchmaking success fees (32%), sponsor subscriptions for business plan filter service (24%), analysis and consulting for business plans (22%) and educational seminars (18%).”

Focusing on entrepreneurial development does not mean dismissing the notion of small business health. We firmly believe that a healthy small business sector is imperative for entrepreneurial growth, especially at the minority level. Not only are small businesses significant customers of many entrepreneurial goods and services, they also act as a recruiting ground for entrepreneurial companies.

Creating an environment where minorities become technology literate, where minority business owners have easier access to cash and other vital resources and the general population is trained in business creation and development strategies is an important step in promoting minority entrepreneurial development. Indirectly, such programs as Los Angeles’ Operation Hope, an economic and business development program targeting the Los Angeles Inner City, bears watching.

In the Fall of 2000, Operation Hope opened the first of its three cyber cafes in Los Angeles’ inner city to provide the local residents with high technology skills, job placement and a convenient location to conduct business. The Cyber Café will offer six courses through UCLA Extension after which program participants will receive a certificate qualifying them to hold jobs in the high-tech sector.

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31 eFiltro business plan.
Operation Hope also has partnered with a provider of e-learning courses to provide 4,500 scholarships over three for those interested in taking internet learning courses provided by the e-learning partner.
RECOMMENDATIONS

If technology and technology related businesses continue to be the largest recipients of venture capital, it is imperative that the pool of technology professionals have more representation from African Americans and Hispanics. But this is a long-term strategy. Technology programs in schools that cater to minority programs need to be strengthened. Similarly non-curricular activities such as science camps, scientific expeditions and science-related work and internships programs need to be put in place so that all minority groups can access them.

The following strategies have the potential of providing paybacks in the immediate future and long term.

♦ Entrepreneurs-in-Residence:
Many mainstream venture funds have been using these Entrepreneur in Residence (EIR) programs to attract entrepreneurs and help them design and launch their businesses. The advantages of such programs are that they don’t require large cash outlays and are collaborative in nature. They usually involve venture capitalists working closely with entrepreneurs to create a business plan, put together a management team and finance the seed round. The probability that these projects turn into real businesses is very high. However, such programs require that venture funds have the expertise in house or can quickly call on external sources for help. Almost every major venture capital fund, including Accel Partners, Kleiner Perkins Caufield & Byers, Mayfield Fund and New Enterprise Associates, has an EIR program in place.

♦ Technology Incubators:
Incubators historically have been a real estate resource shared by small businesses. Incubator tenants also share a variety of business services. Universities expanded the notion of the incubator to directly include
commercialization of technology. Such initiatives have resulted in such projects as New Haven’s Science Park, which was partly funded by Yale University, and incubator programs at Renssalaer Polytechnic, Worcester Polytechnic and others.

We believe that incubator programs that bring together technologies looking for commercialization and entrepreneurs, even if they are not formally trained in technology, have the capability of bearing quick results. Not only do they make key technologies available to potential entrepreneurs, they also help entrepreneurs become more familiar with the technology in the setting it was born.

A few venture funds, notably Kleiner Perkins Caufield & Byers, New Enterprise Associates and the Mayfield Fund also experimented with the notion of a venture incubator. An affiliated feeder fund, Onset Partners, jointly financed by the three funds, was given responsibility to provide the seed stage financing and development to early-stage ideas. The incubated projects then were eligible to receive follow-on financing from Kleiner Perkins, NEA and Mayfield.

Small technology-oriented incubators that have ties with late stage funds may be ideal for creating minority-owned businesses that then become eligible for additional financing.

♦ Social Venturing:

There is a need for patient capital to create sustainable businesses and jobs in minority communities. While this capital may not deliver enormous financial returns in the short term, it has the capability of creating a pool of qualified professionals and companies that then can grow larger.

A model for such patient investing is Silicon Valley Community Ventures (SVCV), which is backed by such venture capitalists as John Doerr of Kleiner Perkins
Caufield & Byers, Jim Breyer of Accel Partners, and Gib Myers of the Mayfield Fund. SVCV offers comprehensive resources to entrepreneurs through advising, a resource network, loans and equity financing. The business advisory program provides advice and assistance to low-income area businesses. While this Inner City program situated in the San Francisco/San Jose Bay area does not specifically target minorities, nearly 50 percent of its clients are minority-owned businesses.

On-Line Minority Business Marketplace:

Events to bring together traditional minority businesses and capital providers have generally proved abortive because of the lack of understanding between the two and the failure to follow up. Exit interviews at Dow Jones Entrepreneurship Conferences and recent events co-sponsored by the NMSDC have shown that most minority entrepreneurs are not familiar with the expectations of capital providers. Similarly, capital providers often do not have the structural or programmatic flexibility to accommodate the financial structures of most minority-owned businesses. We are confident that a “minority business marketplace” site could provide minority groups access to a broad range of business information, market opportunities and financial services and tools designed to help these companies grow and succeed.

We see this site offering business and entrepreneurial news and information to each of the minority groups. We also see this site offering tools to improve the financial competitiveness and reporting abilities of minority-owned businesses as well as organizational and management tools. The Minority Business Marketplace site should contain a “uniform disclosure form,” a single document providing all the information that is needed to qualify for loans or participate in certified purchasing programs. The mechanism to generate the disclosure form should be an interactive, tutorial-like process through which the minority entrepreneur would be assisted in identifying his needs and refining the plans for his business. We also see the site working with service providers, such as
insurance, law and accounting firms and others, to supply regular and cost-effective consulting services to minority-owned businesses.

♦ **Minority Venture Consortium:**

As noted above, minority venture capital firms are typically small and with limited technological and management experience. However, collectively, such funds do command a significant pool of capital. In order to maximize the impact of that pool of capital, a consortium should be established to provide (a) technical and management support (through fellowships, training programs and workshops), (b) a mechanism for the early identification of promising technology companies and (c) a mechanism for pooling resources so that sufficient capital and management and technological assistance is made available to adequately support such promising companies. The fellowship aspect of such a program could be modeled on the Kauffman Fellows Program.
Rationale for Focus of Minority Entrepreneurship Scan

In the discussions to define the scope of the minority entrepreneurship scan, it was agreed that we would discuss entrepreneurship from a public policy perspective, and, in particular, we would focus on those aspects of entrepreneurship which

- contribute to economic development and community growth,
- create jobs,
- build businesses, and
- lead to wealth creation, not simply for an individual but for a larger community.

We looked at entrepreneurial activity in the mainstream and found that the companies that fulfilled these criteria the best over the last two decades were entrepreneurial companies in the technology sector. Technology companies, ranging from Lotus and Microsoft to eBay and Amazon, have been among the most efficient in building lasting businesses, creating jobs and creating community wealth.

Non technology industries, in such areas as traditional manufacturing and retailing, have had significant companies but their need for high levels of capital and their relatively slower rate of growth puts them on a lower priority when it comes to policymaking.

We also found that, particularly as part of the minority entrepreneurship landscape, mergers and acquisitions, corporate divestitures and roll-ups – while legitimate and significant areas of private equity activity – were more about dealmaking than entrepreneurship. The short-term impact of these activities on jobs and business-building was often harmful to a local economy and to unskilled
labor. As a result we felt that start-ups should be the major focus of the entrepreneurial scan.

Based on our observations we suspected that different ethnic groups had different rates of success in raising capital for entrepreneurial businesses. When we looked closer we found that it appeared to be true. The data showed that these differential rates of success appeared to be influenced not only by changing demographics but differential participation in education and in business as well. We felt that only by expanding the discussion to discuss changing demographics and the differential rates of participation in various areas could we get a more complete picture of minority entrepreneurship today.