# Entrepreneurial Confidence Index - ECI Analysis

**Second Quarter 2003**
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During the second quarter, more than 12,500 emerging companies, institutions and private investors participated in the Entrepreneurial Confidence Index (ECI) at www.vfinance.com, the Internet's leading private equity portal. The results are an extremely useful tool for early identification of industries and sectors that will lead the economy's future growth.

As the US economy remained mired in a sluggish recovery characterized by job losses and weak output growth, it has rarely been more important to recognize the importance of entrepreneurship. Entrepreneurs are the driving force behind the innovation that generates economic growth. That drive will be needed for the economy to generate the employment growth needed to boost the economy in the second half of the year. Some of the most relevant findings include:

- Entrepreneurial activity surged 52% in the second quarter of 2003 compared with the second quarter of 2002. The ECI reported increases in 11 of 28 major industry sectors and 150 of 289 sub-sectors. The ECI also showed a 4% increase in entrepreneurial activity over Q1 2003.
- The major sectors (large groupings of industries) generating the most activity in Q2, 2003 were: **Computer Software and Services (CSS)**, **Leisure** and **Real Estate.** CSS had, by far, the largest number of individuals searching for financing and accounted for 13.9% of the total universe, Leisure generated 8.8% of the inquiries and Real Estate 8.2%. The most important findings from this analysis are:
    - Interest in **Real Estate** appears to be waning; its share went from 9.4% of all inquiries a year ago to 8.2%, the second-largest decline of any sector. **Real Estate** is still popular, but less so than a year ago.
    - Interest in software has revived. **Educational Software** and **Internet & Intranet Software and Services** both saw large increases in their share of all responses compared with the first quarter.
    - Interest in **Retail** remains strong. Inquiries about the **Retail** and **Specialty Retail** sectors together accounted for 12.3% of all inquiries, up from 8.2% a year ago.
- The survey also revealed the most popular of the 289 sub-sectors we track in Q2 2003 were: Internet/Intranet Software (3.2% of overall activity); Miscellaneous Specialty Retail (3.1%); Miscellaneous Entertainment (2.5%); Real Estate Development (2.3%); and Property Investment & Management (2.0%).

## Analysis by Sector

- The sectors with the largest increase in activity when compared to the same three-month period of 2002 were **Food, Specialty Retail, Retail, Diversified Services, and Materials and Construction.** Each of these sectors saw their share of inquiries increase by more than one percentage point. Together, these five sectors accounted for nearly one half (43%) of the total increase in inquiries for the quarter. These results suggest a strong focus on the consumer sector of the economy. Taken together, four major consumer-related sectors: Retail, Specialty Retail, Food and Leisure accounted for more than 27% of all inquiries. **The consumer has been the mainstay of the economic expansion and entrepreneurs are seeking to take advantage by starting consumer-related businesses.**
- The sectors that showed the greatest increases compared to the first quarter of 2003 were **Retail**, **CSS**, **Specialty Retail** and **Food**. On the negative side, there were large declines in the share of inquiries for several large industries including **Energy**, **Manufacturing**, **Leisure** and **Transportation**. Together, these four sectors saw their share of all inquiries decline from 16.3% to 14%. Transportation and Energy tend to have high barriers to entry, either in the form of capital requirements or oligopolistic (concentrated) structures making them less attractive to entrepreneurs In Leisure, the decline was primarily a result of a large drop in interest in the Lodging sub sector, no surprise given the poor state of the tourism industry.

## Analysis by Sub-Sector

- The sub-sectors showing the strongest growth from Q2 2002 to Q2 2003 focused largely on the consumer side of the economy. The five sub sectors with the largest increases in their share of the total were: Miscellaneous Retail (up 0.85 percentage points in share), Health & Beauty Product Retailing (0.58 percentage points), Personal Services

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(0.53 percentage points), Specialized Health Services (0.48 percentage points), and Clothing Retail (0.43 percentage points). Of the 20 sub sectors with the largest gain, 10 are in consumer-related industries.

- The Sub sectors showing the greatest decline in entrepreneurial interest were a lot more diversified, ranging from: Investment Banking & Brokerage (-0.45 percentage points), to Real Estate Development (-0.47 points), Sporting Activities (-0.62 points), Music Production & Publishing (-0.71 points), and Internet & Intranet Software & Services (-0.88). The decline in Investment Banking is no surprise given the poor performance of the financial services sector in recent years, but the decline in Internet & Intranet Software & Services is somewhat surprising considering the performance of other technology-related sectors (IT consulting saw its share jump 0.18 points for example). Nevertheless, the Internet and Intranet Software and Services sub sector is still the largest single sub sector attracting 3.2 % of all inquiries in the quarter.
- The sub-sectors with the largest gains from the first quarter of 2003 included **Educational Software** where the share of inquiries increased 0.35 percentage points, Major Diversified Media (+0.33 points), Miscellaneous Entertainment (+0.33 points) and Miscellaneous Retail (+0.30 points). With the exception of Media, these have the characteristics of low barriers to entry and relatively diverse structures making them easier for entrepreneurs to enter.
- On the downside, Sub-sectors showing the largest declines versus the previous quarter include, Oil & Gas Exploration & Production (-0.32 percentage points), Professional & Financial Software (-0.38 points), Restaurants (-0.38 points), Lodging (-0.56 points), Miscellaneous General & Special Machinery (-0.56 points).

## Entrepreneurial Confidence

- The Entrepreneurial Confidence Index also measures both **entrepreneur and investor confidence** in the private equity markets nationwide. This quarter's results showed that 57% of entrepreneurs seeking financing are "very confident" they will receive funding. The net confidence (those "very confident" plus those "somewhat confident" minus those "not confident") rose slightly to 69%, from 68% in the first quarter. These are still low readings, reflecting the continuing softness in venture capital funding.
- On the investor side, only 59% of institutional and wealthy private investor respondents indicated they would fund more than two deals this year, down sharply from 70% in the first quarter of 2003. Part of this may be a reaction to the uncertainty that accompanied the Iraq war and its aftermath and part is probably due to the slowdown in merger and IPO activity, providing fewer avenues for exit from investments.

**Chart No. 1 – Percentage contribution by Industry in 2Q 2003**

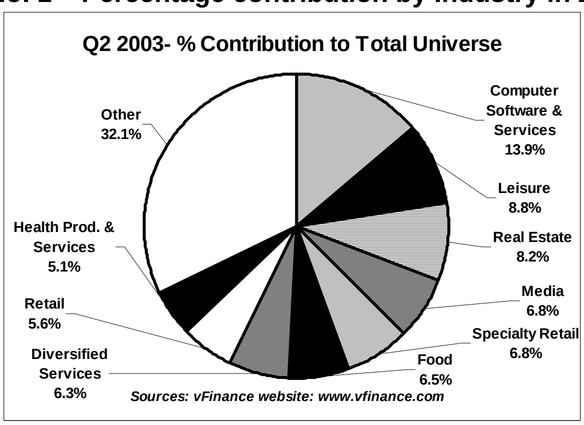



**Chart No. 2 – Q2 2002 vs. Q2 2003 - Major Growth and Decline in Participation by Major Sector.**
The following table presents the top 12 sectors that contribute with over 80% of our universe.

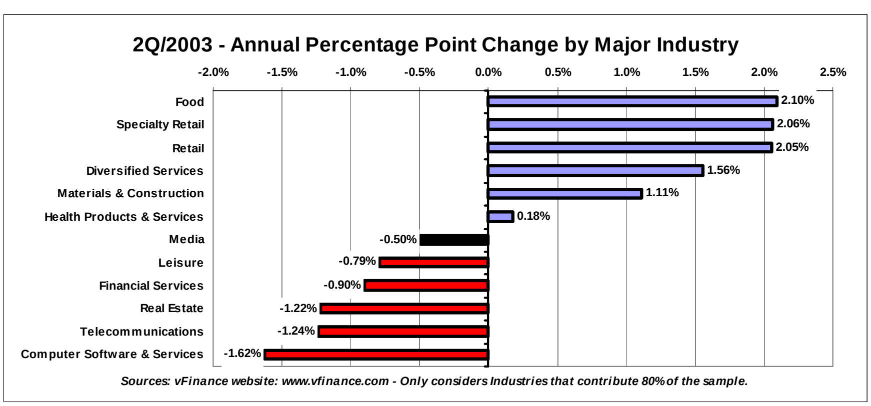


**Chart No. 3 –** Industries w/ largest growth in Entrepreneurial participation.

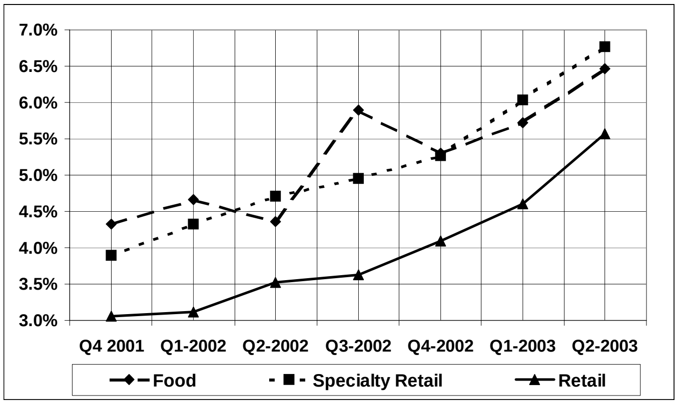
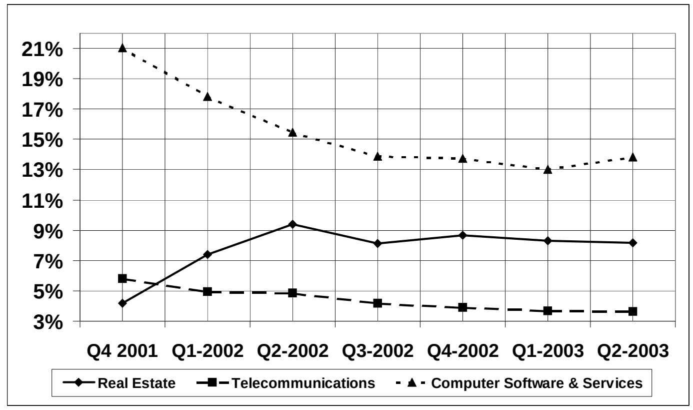



**Chart No. 4** – Industries w/ largest declines in Entrepreneurial participation.




## Top 40 Sub-Sectors with the Highest Growth and Declines – 2Q/2002 vs. 2Q/2003

| Description | Specific | 2Q 2002 | % | 2Q 2003 | % | Diff. Pp | % Chg |
|---|---|---|---|---|---|---|---|
| Specialty Retail | Miscellaneous Retail | 174 | 2.23% | 385 | 3.08% | 0.85% | 121.26% |
| Retail | Health & Beauty Product Retailing | 14 | 0.18% | 95 | 0.76% | 0.58% | 578.57% |
| Diversified Services | Personal Services | 38 | 0.49% | 127 | 1.02% | 0.53% | 234.21% |
| Health Products & Services | Specialized Health Services | 102 | 1.31% | 223 | 1.78% | 0.48% | 118.63% |
| Retail | Clothing | 104 | 1.33% | 220 | 1.76% | 0.43% | 111.54% |
| Materials & Construction | Specialty Contracting & Industrial Maintenance | 15 | 0.19% | 76 | 0.61% | 0.42% | 406.67% |
| Retail | Shoe & Accessory Retailing & Wholesaling | 16 | 0.20% | 70 | 0.56% | 0.35% | 337.50% |
| Food | Beverages - Soft Drinks | 16 | 0.20% | 67 | 0.54% | 0.33% | 318.75% |
| Media | Media - Major Diversified | 115 | 1.47% | 223 | 1.78% | 0.31% | 93.91% |
| Food | Miscellaneous Food Products | 50 | 0.64% | 117 | 0.94% | 0.30% | 134.00% |
| Diversified Services | Management Consulting Services | 32 | 0.41% | 86 | 0.69% | 0.28% | 168.75% |
| Specialty Retail | Miscellaneous Wholesale | 22 | 0.28% | 67 | 0.54% | 0.25% | 204.55% |
| Specialty Retail | Auto Dealers & Distributors | 6 | 0.08% | 41 | 0.33% | 0.25% | 583.33% |
| Diversified Services | Marketing & Public Relations Services | 18 | 0.23% | 60 | 0.48% | 0.25% | 233.33% |
| Food | Food Wholesale - to Restaurants | 30 | 0.38% | 79 | 0.63% | 0.25% | 163.33% |
| Food | Diversified Foods - Other | 42 | 0.54% | 97 | 0.78% | 0.24% | 130.95% |
| Food | Sugar & Confectionery | 9 | 0.12% | 44 | 0.35% | 0.24% | 388.89% |
| Food | Diversified Foods - Major | 14 | 0.18% | 52 | 0.42% | 0.24% | 271.43% |
| Specialty Retail | Book & Entertainment Software Retailing & Dist. | 11 | 0.14% | 47 | 0.38% | 0.24% | 327.27% |
| Automotive & Transport Equipment | Auto Parts | 44 | 0.56% | 99 | 0.79% | 0.23% | 125.00% |
| Computer Software & Services | Other Application Software | 85 | 1.09% | 112 | 0.90% | -0.19% | 31.76% |
| Real Estate | Property Investment & Management | 174 | 2.23% | 253 | 2.02% | -0.20% | 45.40% |
| Telecommunications | Internet & Online Service Providers | 56 | 0.72% | 64 | 0.51% | -0.20% | 14.29% |
| Health Products & Services | Medical Appliances & Equipment | 45 | 0.58% | 45 | 0.36% | -0.22% | 0.00% |
| Electronics & Miscellaneous Technology | Miscellaneous Electronics | 69 | 0.88% | 82 | 0.66% | -0.23% | 18.84% |
| Computer Software & Services | Database & File Management Software | 55 | 0.70% | 59 | 0.47% | -0.23% | 7.27% |
| Leisure | Adult Entertainment | 64 | 0.82% | 73 | 0.58% | -0.24% | 14.06% |
| Computer Software & Services | Educational Software | 85 | 1.09% | 101 | 0.81% | -0.28% | 18.82% |
| Telecommunications | Wireless | 87 | 1.11% | 102 | 0.82% | -0.30% | 17.24% |
| Aerospace & Defense | Aerospace/Defense - Products | 56 | 0.72% | 52 | 0.42% | -0.30% | -7.14% |
| Financial Services | Mortgage Banking & Related Services | 57 | 0.73% | 53 | 0.42% | -0.31% | -7.02% |
| Leisure | Restaurants | 113 | 1.45% | 138 | 1.10% | -0.34% | 22.12% |
| Financial Services | Services to Financial Companies | 60 | 0.77% | 50 | 0.40% | -0.37% | -16.67% |
| Health Products & Services | Medical Instruments & Supplies | 67 | 0.86% | 59 | 0.47% | -0.39% | -11.94% |
| Consumer Products - Non-Durables | Miscellaneous Non-Durable Consumer Goods | 99 | 1.27% | 110 | 0.88% | -0.39% | 11.11% |
| Energy | Oil & Gas Exploration & Production | 55 | 0.70% | 34 | 0.27% | -0.43% | -38.18% |
| Financial Services | Investment Banking & Brokerage | 67 | 0.86% | 51 | 0.41% | -0.45% | -23.88% |
| Real Estate | Real Estate Development | 213 | 2.73% | 282 | 2.25% | -0.47% | 32.39% |
| Leisure | Sporting Activities | 189 | 2.42% | 225 | 1.80% | -0.62% | 19.05% |
| Media | Music Production & Publishing | 203 | 2.60% | 236 | 1.89% | -0.71% | 16.26% |
| Computer Software & Services | Internet & Intranet Software & Services | 319 | 4.08% | 400 | 3.20% | -0.88% | 25.39% |

*Sources: vFinance website: www.vfinance.com - Only considers Industries that contribute to 80% of the sample.*
*p.p. Percentage Point*

**Methodology:** This analysis only considered 12 sectors and 116 sub-sectors, which constitute 80% of the overall universe of industries and sectors. The variations are analyzed on a weighted manner; therefore, any increase or decrease shown is the result of changes in the participation of a specific industry or sector within the overall universe.

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