

Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

WATERSIDE CAPITAL CORP  
Form 10-Q  
November 14, 2001

SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 20549  
-----

Form 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (D) OF  
THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTER ENDED  
SEPTEMBER 30, 2001

COMMISSION FILE NO.: 333-36709  
-----

WATERSIDE CAPITAL CORPORATION  
(Exact name of registrant as specified in its charter)

VIRGINIA  
(State of Incorporation)

54-1694665  
(I.R.S. Employer Identification Number)

300 EAST MAIN STREET, SUITE 1380, NORFOLK, VIRGINIA  
(Address of principal executive office)

23510  
(Zip Code)

(757) 626-1111  
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and has been subject to the filing requirements for the past 90 days.

Yes [X] No

As of September 30, 2001, the registrant had issued and outstanding 1,581,430 shares of Common Stock, \$1.00 par value.

1

WATERSIDE CAPITAL CORPORATION  
FORM 10-Q

Table of Contents

	Page Number
PART I. FINANCIAL INFORMATION	
Item 1. Balance Sheets as of June 30, 2001 and September 30, 2001 (unaudited)	
Statements of Operations for the Three Months Ended September 30, 2000 and 2001 (unaudited)	

Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

Statements of Changes in Stockholders' Equity for the Three Months Ended September 30, 2000 and 2001 (unaudited)

Statements of Cash Flows for the Three Months Ended September 30, 2000 and 2001 (unaudited)

Notes to Financial Statements (unaudited)

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

PART II. OTHER INFORMATION

SIGNATURES

2

PART II. OTHER INFORMATION:

ITEM 1. LEGAL PROCEEDINGS

The Company is not a party to any material legal proceedings.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS

Not applicable.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

None.

3

WATERSIDE CAPITAL CORPORATION

Balance Sheets

June 30, 2001 and September 30, 2001

-----

Ju

-----

Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

Assets:

Investments in portfolio companies, at fair value (note 2):

Equity securities	\$
Debt securities	
Options and warrants	

Total investments, cost of \$41,702,728 and \$39,376,039  
at June 30, 2001 and September 30, 2001, respectively

Current assets:

Cash and cash equivalents
Current portion of dividends receivable
Interest receivable
Notes receivable
Refundable income taxes
Prepaid expenses
Other current assets

Total current assets

Dividends receivable, excluding current portion
Property and equipment, net
Deferred income taxes
Deferred financing costs, net

Total assets

Liabilities and Stockholders' Equity:

Current liabilities:

Accounts payable	\$
Accrued interest	
Accrued expenses	

Total current liabilities

Debentures payable

Total liabilities

Stockholders' equity:

Common stock, \$1 par value, 10,000,000 shares authorized, 1,581,430 issued and outstanding
Preferred stock, \$1 par value, 25,000 shares authorized, no shares issued and outstanding
Additional paid-in capital
Net unrealized depreciation on investments, net of income taxes
Undistributed accumulated earnings

Total stockholders' equity

Commitments and contingencies

Total liabilities and stockholders' equity

Net asset value per common share

See accompanying notes to financial statements.

Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

4

WATERSIDE CAPITAL CORPORATION

Unaudited Statements of Operations

Three-months ended September 30, 2000 and 2001

	2000
Operating income:	
Dividends	\$ 714,34
Interest on debt securities	260,45
Interest on cash equivalents	6,59
Fee and other income	112,04
	-----
Total operating income	1,093,43
	-----
Operating expenses:	
Salaries and benefits	250,53
Legal and accounting	42,38
Interest expense	463,01
Other operating expenses	104,99
	-----
Total operating expenses	860,93
	-----
Net operating income before income taxes	232,50
Income tax benefit	(149,00)
	-----
Net operating income	381,50
Realized loss on investments, net of income tax benefit of \$670,000	
Change in unrealized depreciation on investments, net of income tax expense (benefit) of \$(433,000) and \$814,000 for 2000 and 2001, respectively	(709,56)
	-----
Net increase (decrease) in stockholders' equity resulting from operations	\$ (328,05)
	=====
Net increase (decrease) in stockholders' equity resulting from operations per share - basic and diluted	\$ (0.2)
	=====

See accompanying notes to financial statements.

5

Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

WATERSIDE CAPITAL CORPORATION

Unaudited Statements of Changes in Stockholders' Equity

Three-months ended September 30, 2000 and 2001

	Common stock		Additional paid-in capital	Net unrea deprecia on invest
	Shares	Amount		
Balance at June 30, 2000	1,581,430	\$ 1,581,430	\$ 14,618,719	\$ (1,216
Net operating income	-	-	-	-
Change in net unrealized depreciation on investments, net of income taxes	-	-	-	(709
Balance at September 30, 2000	1,581,430	\$ 1,581,430	\$ 14,618,719	\$ (1,925
Balance at June 30, 2001	1,581,430	\$ 1,581,430	\$ 14,618,719	\$ (7,464
Net operating income	-	-	-	-
Net realized loss on investments, net of income taxes	-	-	-	-
Change in net unrealized depreciation on investments, net of income taxes	-	-	-	1,331
Balance at September 30, 2001	1,581,430	\$ 1,581,430	\$ 14,618,719	\$ (6,132

See accompanying notes to financial statements.

6

WATERSIDE CAPITAL CORPORATION

Unaudited Statements of Cash Flows

Three months ended September 30, 2000 and 2001

Cash flows from operating activities:

Net increase (decrease) in stockholders' equity resulting from operations

\$

Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

Adjustments to reconcile net increase (decrease) in stockholders' equity resulting from operations to net cash used in operating activities:

Unrealized depreciation (appreciation) on investments  
Realized loss on investments  
Accretion of preferred stock and loan investments  
Depreciation and amortization  
Deferred income tax expense (benefit)  
Changes in assets and liabilities increasing (decreasing)  
cash flows from operating activities:  
Dividends receivable  
Interest receivable  
Refundable income taxes  
Prepaid expenses and other current assets  
Accounts payable and accrued expenses

Net cash used in operating activities

Cash flows from investing activities:

Investments in equity securities made  
Investments in debt securities made  
Principal collected on debt securities  
Issuance of note receivable  
Proceeds from collection of note receivable  
Proceeds from sales of investments  
Acquisition of property and equipment

Net cash provided by (used in) investing activities

Cash flows from financing activities:

Repayments of lines of credit  
Proceeds from debentures payable  
Payment of deferred financing costs

Net cash provided by financing activities

Net increase (decrease) in cash and cash equivalents

Cash and cash equivalents, beginning of year

Cash and cash equivalents, end of period

Supplemental disclosure of cash flow information:

Cash paid during the period for interest

Cash paid during the period for income taxes

See accompanying notes to financial statements.

WATERSIDE CAPITAL CORPORATION

Notes to Financial Statements

June 30, 2001 and September 30, 2001 (Unaudited)

## Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

### (1) Unaudited Interim Financial Information

In the opinion of management, the accompanying unaudited interim financial statements of Waterside Capital Corporation (the Company) are prepared in accordance with generally accepted accounting principles (GAAP) for interim financial information and pursuant to the requirements for reporting on Form 10-Q and Article 10 of Regulation S-X. Accordingly, certain disclosures accompanying annual financial statements prepared in accordance with GAAP are omitted. In the opinion of management, all adjustments, consisting of normal recurring accruals necessary for the fair presentation of financial statements for the interim period, have been included. The current period's results of operations are not necessarily indicative of results that ultimately may be achieved for the year. The interim financial statements and notes thereto should be read in conjunction with the financial statements and notes thereto included in the Company's Form 10-K as of and for the year ended June 30, 2001, as filed with the Securities and Exchange Commission.

### (2) Description of Business

The Company was incorporated in the Commonwealth of Virginia on July 13, 1993 and is a closed-end investment company licensed by the Small Business Administration (the SBA) as a Small Business Investment Corporation (SBIC). The Company makes equity investments in, and provides loans to, small business concerns to finance their growth, expansion and development. Under applicable SBA regulations, the Company is restricted to investing only in qualified small business concerns as contemplated by the Small Business Investment Act of 1958.

### (3) Investments

Investments are carried at fair value, as determined by the Executive Committee of the Board of Directors. The Company, through its Board of Directors, has adopted the Model Valuation Policy, as published by the SBA, in Appendix III to Part 107 of Title 12 of the Code of Federal Regulations (the Policy). The Policy, among other things, presumes that loans and investments are acquired with the intent that they are to be held until maturity or disposed of in the ordinary course of business. Except for interest-bearing securities which are convertible into common stock, interest-bearing securities are valued at an amount not greater than cost, with unrealized depreciation being recognized when value is impaired. Equity securities of private companies are presumed to represent cost unless the performance of the portfolio company, positive or negative, indicates otherwise in accordance with the Policy guidelines. The fair value of equity securities of publicly traded companies are generally valued at their quoted market price discounted due to the investment size or market liquidity concerns and for the effect of restrictions on the sale of such securities.

(Continued)

WATERSIDE CAPITAL CORPORATION

Notes to Financial Statements

June 30, 2001 and September 30, 2001 (Unaudited)

---

## Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

Discounts can range from 0% to 40% for investment size and market liquidity concerns. Actual liquidity discounts in the portfolio at September 30, 2001 ranged from 15% to 40%. Discounts for restriction on the sale of the investments are 15% in accordance with the provisions of the Policy. The Company maintains custody of its investments as permitted by the Investment Company Act of 1940.

Investments consist primarily of preferred stock and debt securities obtained from portfolio companies in accordance with SBIC investment regulations. The financial statements include securities valued at \$33,686,908 and \$33,505,668 at June 30, 2001 and September 30, 2001 (87.8% and 87.1% of assets), respectively. The valuation process completed by management includes estimates made by management and the Executive Committee in the absence of readily ascertainable market values. These estimated values may differ significantly from the values that would have been used had a ready market for the securities existed, and those differences could be material.

9

### WATERSIDE CAPITAL CORPORATION

#### Unaudited Schedule of Portfolio Investments

June 30, 2001 and September 30, 2001

-----  
 The Company's investment portfolio at June 30, 2001 consisted of the following:

Equity Securities:	Number of shares
Publicly Traded Companies:	
Avery Communications, Inc. Common Stock	245,000
Avery Communications, Inc. Common Stock (a)	190,167
Avery Communications, Inc. Preferred Stock	1,250,000
Netplex Group, Inc. Common Stock	66,400
Netplex Group, Inc. Preferred Stock	1,500,000
Tangent Solutions, Inc. (formerly Electronic Business Systems, Inc.) Common Stock (b)	500,000
Tangent Solutions, Inc. (formerly Electronic Business Systems, Inc.) Common Stock (b)	1,423,821
Primal Solutions, Inc. Common Stock	475,167
Private Companies:	
Real Time Data Management Services, Inc. Preferred Stock	300
Delta Education Systems, Inc. Preferred Stock	1,625
Diversified Telecom, Inc. Preferred Stock (c)	1,500
Crispies, Inc. Preferred Stock	400
Triangle Biomedical Sciences Preferred Stock (c)	2,100
JMS Worldwide, Inc. Preferred Stock	1,500
EPM Development Systems Corp. Preferred Stock	1,500
Fire King International Preferred Stock	2,000
CCT Holdings (formerly SECC) Common Stock	840,000
Eton Court Asset Management, Ltd. Preferred Stock	1,000
Fairfax Publishing Co., Inc. Preferred Stock	1,100
DigitalSquare.com Convertible Preferred Stock	1,210,739



Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

AnswerNet, Inc. Preferred Stock	550
AnswerNet, Inc. Preferred Stock	700
ISR Solutions, Inc. Preferred Stock	500
Capital Markets Group, Inc. Preferred Stock (c)	1,500
Jubilee Tech International, Inc. Convertible Preferred Stock (c)	2,200,000
VentureCom, Inc. Convertible Preferred Stock	278,164
Phoenix Fabrications, Inc. Preferred Stock (c)	400
AmeriComm Direct Marketing LLC Preferred Stock	27,696
Signius Investment Corporation Common Stock	2,059

Total equity securities

Debt Securities:

-----

Maturity

-----

Avery Communications, Inc. Convertible Note	12/10/02	\$
Extraction Technologies of VA, LLC (c) (d)	7/22/03	
Extraction Technologies of VA, LLC (c) (d)	8/31/04	
Extraction Technologies of VA, LLC (c) (d)	11/2/04	
Extraction Technologies of VA, LLC (c) (d)	2/7/05	
Extraction Technologies of VA, LLC (c) (d)	2/25/05	
Extraction Technologies of VA, LLC (c) (d)	3/14/05	
JMS Worldwide, Inc.	7/31/03	
Diversified Telecom, Inc. (c)	Demand	
Diversified Telecom, Inc. (c)	5/19/02	
ISR Solutions, Inc.	6/30/04	
Fire King International	Demand	
TABET Manufacturing Co., Inc.	12/31/04	
National Assisted Living, LP (c)	12/31/04	
New Dominion Pictures LLC	4/30/06	

(Continued)

WATERSIDE CAPITAL CORPORATION

Unaudited Schedule of Portfolio Investments

June 30, 2001 and September 30, 2001

-----

Maturity

-----

Mayfair Enterprises, Inc.	7/18/05
DigitalSquare.com (c)	9/15/05
Phoenix Fabrications, Inc.	9/8/05
Kotarides Baking Co. of VA (c)	6/5/01
Kotarides Baking Co. of VA	Demand
AmeriComm Direct Marketing LLC	12/29/05
Triangle Biomedical Sciences	12/8/01
Tangent Solutions, Inc. (formerly Electronic Business	

Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

Systems, Inc.) (b) (c)

Total debt securities

Stock Options and Warrants:	Number of shares	Percentage ownership
-----	-----	-----
Publicly Traded Companies:		
Netplex Group, Inc. (a)	300,000	2.10
Tangent Solutions, Inc. (formerly Electronic Business Systems, Inc.) (a) (b)	98,000	0.63
Private Companies:		
Real Time Data Management Services, Inc.	125	29.41
Delta Education Systems, Inc.	639	39.00
Diversified Telecom, Inc.	8,998	15.00
Crispies, Inc.	524	6.37
Triangle Biomedical Sciences	632,916	12.20
Extraction Technologies of VA, LLC (d)	-	39.00
JMS Worldwide, Inc.	199	5.00
EPM Development Systems Corp.	87	8.00
Fire King International	4	4.00
CCT Holdings (formerly SECC)	150,000	3.15
Eton Court Asset Management, Ltd.	14,943	13.00
Fairfax Publishing Co., Inc.	1,026	20.30
ISR Solutions, Inc.	588,334	5.90
DigitalSquare.com	150,000	-
Answernet, Inc.	69,837	16.50
TABET Manufacturing Co., Inc.	487,500	19.50
National Assisted Living, LP	-	15.00
Capital Markets Group, Inc.	2,294,118	15.00
Jubilee Tech International, Inc.	400,000	1.60
Signius Investment Corporation	12	11.67
VentureCom, Inc.	38,943	0.37
New Dominion Pictures LLC	-	9.00
Mayfair Enterprises, Inc.	-	15.00
Phoenix Fabrications, Inc.	-	25.00
Kotarides Baking Co. of VA	-	13.75
Total options and warrants		
Total investments		

(Continued)

Waterside Capital Corporation

Unaudited Schedule of Portfolio Investments

June 30, 2001 and September 30, 2001

Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

The Company's investment portfolio at September 30, 2001 consisted of the following:

Equity Securities:	Number of shares
<b>Publicly Traded Companies:</b>	
Avery Communications, Inc. Common Stock	245,000
Avery Communications, Inc. Common Stock (a)	190,167
Avery Communications, Inc. Preferred Stock	1,250,000
Netplex Group, Inc. Common Stock	66,400
Tangent Solutions, Inc. (formerly Electronic Business Systems, Inc.) Common Stock (b)	500,000
Tangent Solutions, Inc. (formerly Electronic Business Systems, Inc.) Common Stock (b)	1,423,821
Primal Solutions, Inc. Common Stock	400,167
<b>Private Companies:</b>	
Real Time Data Management Services, Inc. Preferred Stock	300
Delta Education Systems, Inc. Preferred Stock	1,625
Diversified Telecom, Inc. Preferred Stock (c)	1,500
Crispies, Inc. Preferred Stock	400
Triangle Biomedical Sciences Preferred Stock (c)	2,100
EPM Development Systems Corp. Preferred Stock	1,500
Fire King International Preferred Stock	2,000
CCT Holdings (formerly SECC) Common Stock	840,000
Eton Court Asset Management, Ltd. Preferred Stock	1,000
Fairfax Publishing Co., Inc. Preferred Stock	1,100
DigitalSquare.com Convertible Preferred Stock	1,210,739
Answernet, Inc. Preferred Stock	550
Answernet, Inc. Preferred Stock	700
ISR Solutions, Inc. Preferred Stock	500
Capital Markets Group, Inc. Preferred Stock (c)	1,500
Jubilee Tech International, Inc. Convertible Preferred Stock (c)	2,200,000
VentureCom, Inc. Convertible Preferred Stock	278,164
Phoenix Fabrications, Inc. Preferred Stock (c)	400
AmeriComm Direct Marketing LLC Preferred Stock	27,696
Signius Investment Corporation Common Stock	2,059
Netplex Systems, Inc. Preferred Stock	1,000,000
Total equity securities	

Debt Securities:	Maturity
Avery Communications, Inc. Convertible Note	12/10/02
Extraction Technologies of VA, LLC (c) (d)	7/22/03
Extraction Technologies of VA, LLC (c) (d)	8/31/04
Extraction Technologies of VA, LLC (c) (d)	11/2/04
Extraction Technologies of VA, LLC (c) (d)	2/7/05
Extraction Technologies of VA, LLC (c) (d)	2/25/05
Extraction Technologies of VA, LLC (c) (d)	3/14/05
JMS Worldwide, Inc.	7/31/03
Diversified Telecom, Inc. (c)	Demand
Diversified Telecom, Inc. (c)	5/19/02

Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

ISR Solutions, Inc.	6/30/04
Fire King International	Demand
TABET Manufacturing Co., Inc.	12/31/04
National Assisted Living, LP (c)	12/31/04
New Dominion Pictures LLC	4/30/06

12

WATERSIDE CAPITAL CORPORATION

Unaudited Schedule of Portfolio Investments

June 30, 2001 and September 30, 2001

-----

	Maturity
	-----
Mayfair Enterprises, Inc.	7/18/05
DigitalSquare.com (c)	9/15/05
Phoenix Fabrications, Inc. (c)	9/8/05
Kotarides Baking Co. of VA (c)	6/5/01
Kotarides Baking Co. of VA	Demand
AmeriComm Direct Marketing LLC	12/29/05
Triangle Biomedical Sciences	12/8/01
Jubilee Tech International, Inc.	3/21/02
Netplex Group, Inc.	12/31/01
Netplex Group, Inc.	1/28/02

Total debt securities

Stock Options and Warrants:	Number of shares	Percentage ownership	
-----	-----	-----	
Private Companies:			
Real Time Data Management Services, Inc.	125	29.41	\$
Delta Education Systems, Inc.	639	39.00	
Diversified Telecom, Inc.	8,998	15.00	
Crispies, Inc.	524	6.37	
Triangle Biomedical Sciences	632,916	12.20	
Extraction Technologies of VA, LLC (d)	-	39.00	
JMS Worldwide, Inc.	199	5.00	
EPM Development Systems Corp.	87	8.00	
Fire King International	4	4.00	
CCT Holdings (formerly SECC)	150,000	3.15	
Eton Court Asset Management, Ltd.	14,943	13.00	
Fairfax Publishing Co., Inc.	1,026	20.30	
ISR Solutions, Inc.	588,334	5.90	
DigitalSquare.com	150,000	-	
Answernet, Inc.	69,837	16.50	
TABET Manufacturing Co., Inc.	487,500	19.50	

## Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

National Assisted Living, LP	-	15.00
Capital Markets Group, Inc.	2,294,118	15.00
Jubilee Tech International, Inc.	400,000	1.60
Signius Investment Corporation	12	11.67
VentureCom, Inc.	38,943	0.37
New Dominion Pictures LLC	-	9.00
Phoenix Fabrications, Inc.	-	25.00

Total options and warrants

Total investments

- (a) Rule 144A restricted securities.
- (b) This entity filed Chapter 11 bankruptcy on September 1, 2000.
- (c) Entity is in arrears with respect to dividend/interest payments.
- (d) This entity filed Chapter 11 bankruptcy on December 26, 2000.

13

### ITEM 2

#### MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

##### . General

Waterside Capital Corporation ("Waterside" or the "Company") is a specialty finance company located in Norfolk, Virginia. The Company invests in equity and debt securities to finance the growth, expansion and modernization of small private businesses, primarily in the Mid-Atlantic Region. The Company was formed in 1993 as the Eastern Virginia Small Business Investment Corporation. Through June 30, 1996, the Company operated as a development stage company focused primarily on preparation to commence operation. The Company was licensed in 1996 by the Small Business Administration (SBA) as a Small Business Investment Company (SBIC) under the Small Business Investment Act of 1958. In October 1996 the Company made its first portfolio investment. In January 1998 the Company completed its Initial Public Offering (IPO) to raise additional equity to support its growth strategy.

The majority of the Company's operating income is derived from dividend and interest income on portfolio investments and application and processing fees related to investment originations. The remaining portion of the Company's operating income comes from interest earned on cash equivalents. The Company's operating expenses primarily consist of interest expense on borrowings to fund its portfolio growth and payroll and other expenses incidental to operations. Waterside currently has 6 full time employees.

##### . Results of Operations

Comparison of Three Months Ended September 30, 2001 and September 30,

## Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

2000

For the three months ended September 30, 2001, total operating income was \$1,182,000 compared to \$1,093,000 reported during the same period of 2000. The increase in operating income is primarily attributed to the collection of \$75,000 in late fees on a delinquent investment that was repaid during October 2001. The September 30, 2001 quarterly operating income consisted of dividends of \$601,000, interest on debt securities of \$406,000, fee income of \$167,000 and interest on cash equivalents of \$8,000.

Total operating expenses were \$840,000 for the three months ended September 30, 2001, as compared to the \$861,000 reported for the quarter ended September 30, 2000. Total operating expenses for the three months ended September 30, 2001 consisted of interest expense of \$523,000, salaries and benefits of \$193,000, legal and accounting expenses of \$44,000, and other operating expenses of \$80,000. These expenses compared to the amounts reported for the three months ended September 30, 2000, of interest expense of \$463,000, salaries and benefits of \$251,000, legal and accounting expenses of \$42,000, and other operating expenses of \$105,000. The increase in interest expense for the quarter ended September 30, 2001, compared to the quarter ended September 30, 2000 is due to the increased borrowings necessary to fund the Company's investment portfolio. The decrease in salaries and benefits for the quarter ended September 30, 2001, compared to the quarter ended September 30, 2000, is due to the reduction in force of one business development officer and one clerical position. Net operating income was \$418,000 for the three months ended September 30, 2001, compared to the \$382,000 reported for the three months ended September 30, 2000.

14

The realized loss on investments, net of income taxes, of \$1,095,000 for the three months ended September 30, 2001, was primarily due to the realization of the previously recorded unrealized loss related to Tangent Solutions, Inc., (formerly named Electronic Business Systems, Inc., and Triangle Imaging Group, Inc.). The realization was due to a bankruptcy ruling. The increase in unrealized appreciation on investments, net of taxes, of \$1,331,000 for the three months ended September 30, 2001, was due to a combination of the reversal of unrealized depreciation related to Tangent Solutions, Inc., and the recognition of \$540,000 of unrealized appreciation related to The Netplex Group, Inc., investment.

The net increase in stockholders' equity resulting from operations of \$655,000 for the three months ended September 30, 2001, or \$0.41 per share compared favorably to a decrease of \$328,000 or \$0.21 per share for the comparable period ended September 30, 2000.

### . Financial Condition, Liquidity And Capital Resources

At September 30, 2001, the Company's investment portfolio totaled \$33.5 million compared with the \$33.7 million reported at June 30, 2001. For the three months ended September 30, 2001, the Company funded \$280,000 in investments and received proceeds from sales of investments of \$929,000. For the comparable three months ended September 30, 2000, the Company funded \$2,083,000 in new investments.

Net asset value per common share increased to \$8.00 per share at September 30, 2001, from \$7.59 per share reported at June 30, 2001.

## Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

During the three months ended September 30, 2001, net cash used in operating activities was \$358,000 compared to the \$381,000 used during the three months ended September 30, 2000. Cash provided by investing activities was \$674,000 during the three months ended September 30, 2001 as compared to the \$1,612,000 used in investing activities for three months ended September 30, 2000. There were no cash flows provided by financing activities for the three months ended September 30, 2001, compared to the \$1,936,000 provided during the three months ended September 30, 2000. The cash was provided by debenture borrowings from the SBA during the three months ended September 30, 2000, necessary to finance new investments. The cash provided by financing activities was partially offset by repayments on the Company's lines of credit.

### . Events of September 11, 2001

The Company does not have any investments in companies directly affected by the tragic events of September 11, 2001. The Company does not believe that it is possible to assess the indirect effects that these events may have on its portfolio companies. As a result, the Company cannot offer any assurance that direct or indirect consequences of these events will not have an adverse impact on the Company's financial position or results of operations or on the valuation of its portfolio investments.

15

### . Quantitative and Qualitative Disclosure About Market Risk

The Company's business activities contain elements of risk. The Company considers the principal types of market risk to be: risk of lending and investing in small privately owned companies, valuation risk of portfolio, risk of illiquidity of portfolio investments and the competitive market for investment opportunities. The Company considers the management of risk essential to conducting its business and to maintaining profitability. Accordingly, the Company's risk management systems and procedures are designed to identify and analyze the Company's risks, to set appropriate policies and limits and to continually monitor these risks and limits by means of reliable administrative and information systems and other policies and programs.

The Company manages its market risk by maintaining a portfolio of investments that is diverse by industry, geographic area, size of individual investment and borrower. The Company is exposed to a degree of risk of public market price fluctuations as three of the Company's thirty investments are in thinly traded, small public companies, whose stock prices have been volatile. The other twenty-seven investments are in private business enterprises. Since there is typically no public market for the equity interests of the small companies in which the Company invests, the valuation of the equity interests in the Company's portfolio of private business enterprises is based on estimates made by the Company's Executive Committee. In the absence of a readily ascertainable market value, the estimated value of the Company's portfolio of equity interests may differ significantly from the values that would be placed on the portfolio if a ready market for the equity interests existed. Any changes in estimated value are recorded in the Company's statement of operations as "Net unrealized gains (losses)." Each hypothetical 1% increase or decrease in value of the Company's portfolio of investments of \$33.5 million at September 30, 2001, would have resulted in unrealized gains or losses and would have changed net increase in stockholders' equity resulting from operations for the quarter by \$335,000.

## Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

The Company's sensitivity to changes in interest rates is regularly monitored and analyzed by measuring the characteristics of assets and liabilities. The Company utilizes various methods to assess interest rate risk in terms of the potential effect of interest income net of interest expense, the market value of net assets and the value at risk in an effort to ensure that the Company is insulated from any significant adverse effects from changes in interest rates. Based on the model used for the sensitivity of interest income net of interest expense, if the balance sheet were to remain constant and no actions were taken to alter the existing interest rate sensitivity, a hypothetical 100 basis point change in interest rates would have a negligible effect on the net increase in stockholders' equity resulting from operations over a three-month horizon. Although management believes that this measure is indicative of the Company's sensitivity to interest rate changes, it does not adjust for potential changes in credit quality, size and composition of the balance sheet and other business developments that could affect operating results. Accordingly, no assurances can be given that actual results would not differ materially from the potential outcome simulated by this estimate.

16

### . Forward-Looking Statements

Included in this report and other written and oral information by management from time to time, including reports to shareholders, quarterly and semi-annual shareholder letters, filings with the Commission, news releases and investor presentations, are forward-looking statements about business objectives and strategies, market potential, its available capital resources, including SBA leverage, the Company's ability to expand the geographic scope of its investments, the quality of the Company's due diligence efforts, its financing plans, its vendors, suppliers, and portfolio companies, future financial performance and other matters that reflect management's expectations as of the date made.

Except for historical information, all of the statements, expectations and assumptions contained in the foregoing are "forward-looking statements" (within the meaning of the Private Securities Litigation Reform Act of 1995) that involve a number of risks and uncertainties. When the Company used words such as "believes," "expects," "anticipates," "intends," "plans," "estimates," "should," "likely," or similar expressions, the Company is making a forward-looking statement. It is possible that the assumptions made by management - including, but not limited to, the average maturity of our investments, the potential to realize investment gains as these investments mature, investment opportunities, results, performance or expectations - may not materialize. Actual results may differ materially from those projected or implied in any forward-looking statements. In addition to the above factors, other important factors that may affect the company's performance include: the risks associated with the performance of the Company's portfolio companies, dependencies on key employees, interest rates, the level of economic activity, and competition, as well as other risks described from time to time in the Company's filings with the Securities Exchange Commission, press releases, and other communications. The Company disclaims any intent or obligation to update these forward-looking statements, whether as a result of new information, future events, or otherwise.

17



Edgar Filing: WATERSIDE CAPITAL CORP - Form 10-Q

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Company has duly caused this Form 10-Q to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Norfolk, Commonwealth of Virginia on the 13th day of November 2001.

WATERSIDE CAPITAL CORPORATION

By /s/ J. Alan Lindauer

-----

J. Alan Lindauer  
President and Principal Executive Officer

By /s/ Gerald T. McDonald

-----

Gerald T. McDonald  
Principal Financial Officer