

KEATING CAPITAL  
**NEWS**

2nd Quarter 2009

Equity Partners for  
Companies Primed to Become Public™

## The Case for Micro-cap Stocks

There is an enormous audience of both institutional and individual investors actively seeking to identify small, undiscovered public stock gems. This group includes over 30 million online investors in the U.S. who view investing in micro-cap stocks (which we define as stocks and companies with market capitalizations below \$250 million) as a form of "public venture capital." Institutional investors who focus on small/micro-caps are aware of the following:

- ◆ First, from 1926 to 2006, small cap stocks had a compound return of 12.21% compared to 10.26% for the S&P 500—an annual outperformance of nearly 200 basis points over an 80-year period.

- ◆ Second, the majority of top performing stocks (as measured by total return and with a minimum starting market cap of at least \$50 million) in any 10-year period are predominantly small caps. For example, of the 25 top performing stocks from 1998-2008, 10 stocks had starting market caps below \$100 million; an additional six stocks had market caps between \$100 and \$200 million.

Abundant academic research conclusively demonstrates that small cap stocks systematically outperform large cap stocks, even after adjusting for risks as defined within the framework of the capital asset pricing model.

Savvy investors know that they have to look

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Keating Investments, LLC is a Denver-based SEC registered investment adviser founded in 1997. The firm is the investment adviser to Keating Capital, a closed-end fund that makes minority, non-controlling equity investments in private businesses that are seeking growth capital and are committed to, and capable of, becoming public.



# NASDAQ OMX Selects Morningstar to Provide Equity Research Profile Reports On All NASDAQ-Listed Companies

**N**EW YORK/CHICAGO, June 8, 2009 - The NASDAQ OMX Group, Inc. (NASDAQ: NDAQ), the world's largest exchange company, and Morningstar, Inc. (NASDAQ: MORN), a leading provider of independent investment research, have entered into an exclusive agreement

for Morningstar to provide equity research profile reports on more than 3,600 NASDAQ OMX-listed companies.

With the Morningstar Profile Report, NASDAQ OMX will now be able to provide all NASDAQ OMX companies with basic research coverage at no cost to the issuer. This is particularly important for many small- and mid-cap companies that have seen their research coverage shrink or disappear altogether. There are currently approximately 1,400 public companies in the United States that do not have any research coverage.

The Morningstar Profile Report will include a lengthy company profile, comprehensive data about the company and its industry, and industry context written by a Morningstar analyst. It does not include Morningstar's more detailed analyst research report, a Morningstar Rating, or a buy/sell/hold recommendation. ■

MORNINGSTAR									
NASDAQ OMX Group, Inc. NDAQ (Nasdaq)									
Morningstar Rating	Last Price	Fair Value	Consider Buy	Consider Sell	Uncertainty	Economic Moat	Stewardship Grade	Industry	Sector
★★★★	23.17	28.00	14.00	56.00	High	None	B	Securities	Financial Services
Per share prices in USD									
NASDAQ OMX's 1Q Results									
<p>By Michael Wong Stock Analyst Analysis covering this company is not over its stock.</p> <p>Rating updated as of June 18, 2009.</p> <p>Current amounts expressed with "T" are in U.S. dollars (USD) unless otherwise denoted.</p> <p>Stock Price</p>		<p><b>Analyst Note</b> Jun. 03, 2009   Michael Wong, CPA NASDAQ OMX reported net income of \$94 million or \$0.44 per diluted share for the first quarter of 2009. Total net cash equity trading revenue on a pro forma basis decreased 25% from a year ago and 15% from last quarter. The decrease in net cash equity trading revenue is the result of a combination of higher liquidity rebates in the United States, flatish volume year over year, and a decrease in volume from the fourth quarter. The company's market data, issuer services, and market technology revenues held up relatively well. They were down on a pro forma basis approximately 3%, 12%, and 9%, respectively, from the previous year. The company is</p> <p>Nasdaq is well known for its leadership position in the listing and trading of technology-related companies. The company strengthened its core U.S. equity trading platform by acquiring the Brut and Innotest EDN several years ago because of mounting competitive concerns about the effect Regulation National Market System would have on it by putting alternative trading systems on more equal ground. Besides U.S. equity trading, through its acquisition of OMX in early 2008, it became the major marketplace for trading in equity and derivatives in the Nordic and Baltic regions of Europe. Additionally, through its acquisition of the Philadelphia Exchange in late 2008, Nasdaq increased its presence in the U.S. options market. Approximately two thirds of the company's net revenue comes from executing stock and derivative trading transactions through its trading platform and the related market transaction data. The other one third of its net</p>							

## The Case for Micro-caps (continued from page 1)

under the radar screen to find undiscovered stocks. The prime hunting ground for many of these investors is the world of micro-cap stocks. Although initially these stocks typically lack both analyst coverage and institutional sponsorship, for many investors size doesn't matter as long as the company has the fundamentals to support a potential doubling of the stock price in three years. A company growing its earnings at 25% with a constant P/E will more than double its value in three years.

Finally, there is a commonly held misperception that all stocks that trade on Nasdaq are "large." Nothing could be further from the truth. Consider the following facts based on Nasdaq data as of June 17, 2009:

- ◆ While the average market cap for a Nasdaq stock is approximately \$1.03 billion, the median market cap was \$124 million. In other words, half of all the stocks that trade on Nasdaq have market caps under \$124 million.



- ◆ Of the 2,965 U.S. stocks that trade on Nasdaq:
  - 2,520 (88%) had market caps under \$1 billion
  - 1,852 (64%) had market caps under \$250 million (our definition of a micro-cap)
  - 1,318 (45%) had market caps under \$100 million
  - 967 (33%) had market caps under \$50 million

The conclusion: Size doesn't matter if the fundamentals are strong and there is a compelling story that will excite public market investors. ■

# OPINION

by  
Timothy J. Keating

## The Hobson's Choice of Reviving Small Business Capital Formation



In his opening remarks to the 2007 Government-Business Forum on Small Business Capital Formation, former SEC Chairman Christopher Cox acknowledged the critical importance of small business to the U.S. economy:

- ◆ "Small firms represent...99.7% of all the employer firms in the United States. They employ half of the entire labor force in the private sector."
- ◆ "Of all the net new jobs created in our country, small business generated between 60 percent and 80 percent in every year during the last decade."

So, one might reasonably ask, if small business capital formation is so important to the U.S. economy, why is it now nearly impossible for small businesses to go public? The answer: one ill-conceived government regulation piled on top of another in the past decade, which collectively have brought public company capital formation to a grinding halt.

The lack of new public companies matters greatly to a capitalist society because the vast majority of value creation, and hence new jobs, occurs *after* these entrepreneurial companies have gone public. To deny access to the public markets for the most promising of private enterprises seeking growth capital is the moral equivalent of eating one's offspring before they have a chance to thrive. Regrettably, we believe the most effective way to revive small business capital formation, i.e. reverse the damage already inflicted by regulatory and legislative malfeasance, is to work through the SEC and Congress.

The blame surely begins with the infamous Sarbanes-Oxley Act of 2002. Originally designed to cover the 1,000 largest public companies, in a wave of Congressional exuberance Sarbox was eagerly extended to

cover all public companies. While we disagree with some of our peers in the small business community about the actual real cost of complying with Sarbox, in the end it doesn't matter. The perception of \$1 million compliance costs for smaller companies trumps the reality of closer to \$100,000 and is enough to set less-informed companies running from public markets.

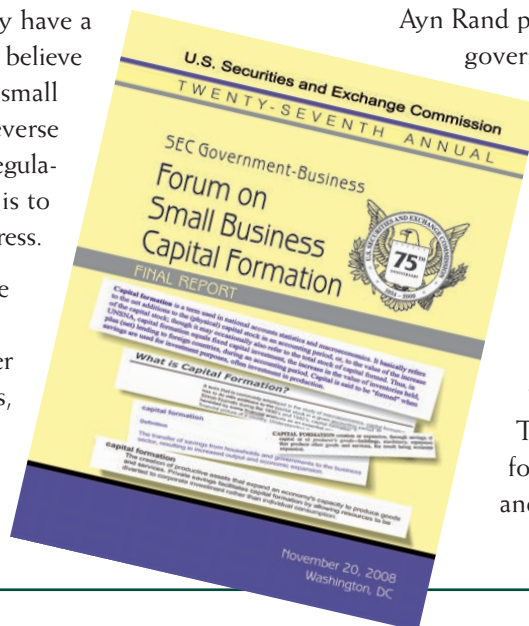
Next on the hit parade came former New York Attorney General Eliot Spitzer's \$1.5 billion "Global Settlement" with Wall Street in 2003 aimed at combating tainted equity research. As part of the settlement, Spitzer forced Wall Street investment banks to spend \$460 million on independent stock research. According to a recent article in *The Wall Street Journal*, it "turns out that many investors couldn't have cared less." The *Journal* goes on to report that in one recent year at Credit Suisse Group, "just 16 retail clients had retrieved reports from the bank's Web site." Spitzer's massive initiative only directly affected a few investors, and perversely, actually decreased the amount of available equity research. Talk about the cure being worse than the disease.

The list goes on and on. For each capital markets "reform" (ahem, regulation) enacted in the past decade, there is a group decrying it as the root of all evil. Regulation Fair Disclosure, Decimalization, Regulation SHO...pick your poison.

Ayn Rand presciently warned about the consequences of government regulation in extremis in her 1957 novel *Atlas Shrugged*. The protagonist, Dagny Taggart, sees society collapse around her as the government asserts control over all industry, while society's most productive citizens, led by the mysterious John Galt, progressively disappear. Galt describes the strike as "stopping the motor of the world" by withdrawing the "minds" that drive society's growth and productivity.

The "minds" behind small business capital formation have increasingly gone on strike and are innovating new solutions.

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## The Hobson's Choice (continued from page 3)

Consider the following:

- ◆ Nasdaq OMX recently announced that it has entered into an agreement with Morningstar to provide a research profile targeted at retail investors for all of the more than 3,600 companies that trade on the exchange-including nearly 900 (25%) that have no analyst coverage at all. [See related article on page 2.]
- ◆ Fidelity Investments and Kohlberg Kravis Roberts & Co. recently announced that they have entered into an agreement to provide Fidelity's brokerage customers to buy into KKR-sponsored IPOs. [See related article below.]
- ◆ At least four new private exchanges (Second Market, Inside Ventures, SharesPost, and XChange) have sprung up in the past few years to fill the IPO void and satisfy investors seeking to participate in investment opportunities of emerging growth companies.

So while we generally applaud innovation in all of its forms, these developments all share one thing in common: they are Band-aids to a badly broken capital formation process. More insidiously, certain of these initiatives run counter to the most important function of an exchange, namely creating a centralized pool of liquidity. Fracturing liquidity serves neither investor nor issuer under any circumstance. In that regard, these liquidity-diffusing solutions are not the long-term fix that is required.

Instead, we think the better solution is to fix the root of the problem: bad and excessive regulation. The recommendations of the 2008 SEC Government-Business Forum on Small Business Capital Formation (<http://sec.gov/info/smallbus/sbforum.shtml>) include 22 securities law changes and a further 15 recommendations on tax issues. We support nearly all of these recommendations. Unfortunately, the very well-intentioned SEC's Office of Small Business Policy headed by Gerry LaPorte seems to be impotent and lost in an otherwise disgraced and dysfunctional agency.

Nevertheless, given the pervasive and highly visible hand of government in the capital markets, we believe that working through the auspices of the Office of Small Business Policy is regrettably a Hobson's choice for those who are serious about reviving small business capital formation. Thus, we encourage all who are involved in the micro-cap public market ecosystem to join the cause of working to agitate for the restoration of rational regulation to our capital markets sooner rather than later. ■

**B**OSTON and NEW YORK, June 8, 2009 - Fidelity Investments® and Kohlberg Kravis Roberts & Co. (KKR) today announced an agreement that enables Fidelity's retail and institutional brokerage customers the opportunity to participate in initial public offerings (IPOs) and follow-on offerings of KKR companies, while providing KKR's capital markets business with a new retail distribution channel.

Through the new relationship, Fidelity will have exclusive access to retail securities that are allocated to KKR in all U.S. public offerings in which KKR participates as an underwriter, including IPOs and follow-on offerings. Those retail securities will be made available to Fidelity's retail brokerage customers as well as to accounts managed by Fidelity's registered investment advisor (RIA), correspondent broker-dealer and other institutional clients. KKR will act as the underwriter of all retail securities that are distributed by Fidelity under the arrangement. ■

