WATERSIDE CAPITAL CORP
Form 10-Q
February 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 DECEMBER 31, 2000

COMMISSION FILE NO.: 333-36709

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

VIRGINIA	54-1694665
(State of incorporation)	(I.R.S. Employer Identification Number)
300 EAST MAIN STREET, SUITE 1380, NORFOLK, VIRGINIA	23510
(Address of principal executive office)	(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 December 31, 2000, the registrant had issued and outstanding 1,581,430 shares of Common Stock, $1.00 par value.

WATERSIDE CAPITAL CORPORATION
FORM 10-Q

Table of Contents

1

PART I. FINANCIAL INFORMATION
ITEM 1.

WATERSIDE CAPITAL CORPORATION

Balance Sheets

June 30, 2000 and December 31, 2000

	June 30, 2000
Assets:	
Investments in portfolio companies, at fair value (note 3):	
Equity securities	$ 23,237,050
Debt securities	8,877,766
Options and warrants	3,752,744
Total investments, cost of $37,826,396 and $40,209,783 at June 30, 2000 and December 31, 2000, respectively	35,867,560
Current assets:	
Cash and cash equivalents	118,314
Dividends receivable	654,767
Interest receivable	222,517

Note receivable	237,550
Refundable income taxes	323,322
Prepaid expenses and other current assets	140,403
Total current assets	1,696,873
Property and equipment, net	167,919
Deferred income taxes, net of valuation allowance of $619,000 at December 31, 2000	650,000
Deferred financing costs, net	716,391
Total assets	$ 39,098,743
Liabilities and Stockholders' Equity:	
Current liabilities:	
Lines of credit	$ 2,200,000
Accounts payable	31,310
Accrued expenses	733,042
Total current liabilities	2,964,352
Debentures payable	19,300,000
Total liabilities	22,264,352
Stockholders' equity:	
Common stock, $1 par value, 10,000,000 shares authorized, 1,581,430 issued and outstanding	1,581,430
Preferred stock, $1 par value, 25,000 shares authorized, no shares issued and outstanding	-
Additional paid-in capital	14,618,719
Net unrealized depreciation on investments, net of income taxes	(1,216,357)
Undistributed accumulated earnings	1,850,599
Total stockholders' equity	16,834,391
Commitments, contingencies and subsequent event (note 4)	
Total liabilities and stockholders' equity	$ 39,098,743
Net asset value per common share	$ 10.65

See accompanying notes to financial statements.

WATERSIDE CAPITAL CORPORATION

Unaudited Statements of Operations

Three months and six months ended December 31, 1999 and 2000

	Three Months Ended December 31, 1999	Three Months Ended December 31, 2000
Operating income:		
Dividends	$ 534,624	$ 645,559
Interest on debt securities	201,952	198,208
Interest on cash equivalents	6,842	1,642
Fee and other income	246,500	93,181
Total operating income	989,918	938,590
Operating expenses:		
Salaries and benefits	211,312	204,836
Legal and accounting	50,000	52,100
Interest expense	268,047	494,644
Other operating expenses	125,118	82,180
Total operating expenses	654,477	833,760
Net operating income before income taxes	335,441	104,830
Income tax benefit	(58,000)	(170,000)
Net operating income	393,441	274,830
Realized gain on investments, net of income taxes of $606,000 for the three and six months ended December 31, 1999	986,153	-
Change in unrealized appreciation (depreciation) on investments, net of income tax expense (benefit) of $615,000 and $159,000 for the three months ended December 31, 1999 and 2000, respectively, and $476,000 and $(274,000) for the six months ended December 31, 1999 and 2000, respectively	1,005,973	(1,369,473)
Net increase (decrease) in stockholders' equity resulting from operations	$ 2,385,567	$ (1,094,643)
Net increase (decrease) in stockholders' equity resulting from operations per share - basic and diluted	$ 1.51	$ (0.69)

See accompanying notes to financial statements.

WATERSIDE CAPITAL CORPORATION

Unaudited Statements of Changes in Stockholders' Equity

Six months ended December 31, 1999 and 2000

	Common stock Shares	Common stock Amount	Additional paid-in capital	Net unrealized appreciation on investments	Undistrib accumula earnin
Balance at June 30, 1999	1,491,937	$1,491,937	$12,769,895	$ 298,434	$ 966,0
6% stock dividend	89,493	89,493	648,824	-	(738,5
Capitalization of undistributed accumulated earnings	-	-	1,200,000	-	(1,200,0
Repayment of stockholders' notes receivable	-	-	-	-	
Net operating income	-	-	-	-	749,5
Net realized gain on investments, net of income taxes	-	-	-	-	986,1
Increase in net unrealized appreciation on investments, net of income taxes	-	-	-	777,651	
Balance at December 31, 1999	1,581,430	$1,581,430	$14,618,719	$1,076,085	$ 763,1

	Common stock Shares	Common stock Amount	Additional paid-in capital	Net unrealized depreciation on investments	Undistri accumul earni
Balance at June 30, 2000	1,581,430	$ 1,581,430	$ 14,618,719	$(1,216,357)	$ 1,850,
Net operating income	-	-	-	-	656,
Increase in net unrealized depreciation on investments, net of income taxes	-	-	-	(2,079,036)	
Balance at December 31, 2000	1,581,430	$ 1,581,430	$ 14,618,719	$(3,295,393)	$ 2,506,

See accompanying notes to financial statements.

WATERSIDE CAPITAL CORPORATION

Unaudited Statements of Cash Flows

Six months ended December 31, 1999 and 2000

	1999
Cash flows from operating activities:	
Net increase (decrease) in stockholders' equity resulting from operations	$ 2,513,345
Adjustments to reconcile net increase (decrease) in stockholders' equity resulting from operations to net cash provided by operating activities:	
Change in unrealized appreciation/depreciation on investments	(1,253,651)
Realized gain on investments	(1,592,153)
Accretion of preferred stock and loan investments	(89,527)
Depreciation and amortization	31,442
Deferred income tax expense (benefit)	510,000
Loss on disposal of property and equipment	828
Changes in assets and liabilities increasing (decreasing) cash flows from operating activities:	
Dividends receivable	(219,362)
Interest receivable	123,821
Refundable income taxes	43,322
Prepaid expenses and other current assets	(205,487)
Accounts payable and accrued expenses	32,275
Deferred revenue	(79,131)
Income taxes payable	399,678
Net cash provided by operating activities	215,400
Cash flows from investing activities:	
Investments in equity securities made	(4,953,425)
Investments in debt securities made	(3,754,189)
Principal collected on debt securities	1,181,842
Proceeds from repayment of stockholders' notes receivable	1,024,000
Proceeds from sales of investments	2,002,724
Acquisition of property and equipment	(3,755)
Proceeds from sale of property and equipment	2,000
Net cash used in investing activities	(4,500,803)

Cash flows from financing activities:	
Proceeds from (payments on) lines of credit	3,700,000
Proceeds from debentures payable	-
Payments in lieu of fractional shares associated with stock dividend	(191)
Payment of deferred financing costs	-
Net cash provided by financing activities	3,699,809
Net decrease in cash and cash equivalents	(585,594)
Cash and cash equivalents, beginning of period	1,269,409
Cash and cash equivalents, end of period	$ 683,815 $
Supplemental disclosure of cash flow information:	
Cash paid during the period for interest	$ 389,911
Cash paid during the period for income taxes	$ -

See accompanying notes to financial statements.

WATERSIDE CAPITAL CORPORATION

Notes to Financial Statements

June 30, 2000 and December 31, 2000 (Unaudited)

---

(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 accompany 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 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.

Discounts can range from 0% to 40% for investment size and market liquidity concerns. Actual liquidity discounts in the portfolio at December 31, 2000 ranged from 11% 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 $35,867,560 and $35,897,910 at June 30, 2000 and December 31, 2000 (91.7% and 91.4% 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.

(4) Subsequent Event

In January 2001, the Company entered into employment agreements with four members of management. These agreements provide for a specified annual base salary and certain discretionary bonuses, and expire on January 31, 2004. Under the agreements, if the Company terminates the employee's employment without cause, the Company is obligated to pay the employee an amount equal to two times the employee's base salary, as then in effect, plus the average of the bonuses received by the employee for each of the two years prior to the date of termination. The Company's maximum potential commitment for termination benefits is approximately $1,000,000.

WATERSIDE CAPITAL CORPORATION

Schedule of Portfolio Investments

June 30, 2000 and December 31, 2000

The Company's investment portfolio at June 30, 2000 consisted of the following:

	Number of shares	Co cont v
Equity Securities:		
Publicly Traded Companies:		
Avery Communications, Inc. Common Stock	245,000	$ 2
Netplex Group, Inc. Common Stock (a)	66,400	4
Netplex Group, Inc. Preferred Stock	1,500,000	1,1
Electronic Business Systems, Inc. (formerly Triangle Imaging Group, Inc.) Convertible Preferred Stock (b) (c)	700	2,0
Electronic Business Systems, Inc. (formerly Triangle Imaging Group, Inc.) Common Stock (b) (c)	500,000	2
Electronic Business Systems, Inc. (formerly Triangle Imaging Group, Inc.) Common Stock (b) (c)	1,423,821	
Private Companies:		
Real Time Data Management Services, Inc. Preferred Stock	300	2
Delta Education Systems, Inc. Preferred Stock	1,625	1,5
Diversified Telecom, Inc. Preferred Stock (c)	1,500	1,5
Crispies, Inc. Preferred Stock	400	3
Triangle Biomedical Sciences Preferred Stock	2,000	1,9
JMS Worldwide, Inc. Preferred Stock	1,500	1,5
EPM Development Systems Corp. Preferred Stock	1,500	1,4
Fire King International Preferred Stock	2,000	2,0
SECC (formerly MilleCom, Inc.) Common Stock	840,000	
Eton Court Asset Management, Ltd. Preferred Stock	1,000	9
Fairfax Publishing Co., Inc. Preferred Stock	1,100	1,0

DigitalSquare.com Preferred Stock	1,210,739	1,5
Answernet, Inc. Preferred Stock	550	3
Answernet, Inc. Preferred Stock	700	3
ISR Solutions, Inc. Preferred Stock	500	4
Capital Markets Group, Inc. Preferred Stock	1,500	1,5
Jubilee Tech International, Inc. Convertible Preferred Stock	2,200,000	1,9
VentureCom, Inc. Preferred Stock	278,164	2,0
Total equity securities		25,1

	Maturity	Cost contri valu
Debt Securities:		
Avery Communications, Inc. Convertible Note	12/10/02	$ 3
Extraction Technologies of VA, LLC	7/22/03	9
Extraction Technologies of VA, LLC	8/31/04	2
Extraction Technologies of VA, LLC	11/2/04	3
Extraction Technologies of VA, LLC	2/7/05	2
Extraction Technologies of VA, LLC	2/25/05	
Extraction Technologies of VA, LLC	3/14/05	
JMS Worldwide, Inc.	7/31/03	9
Diversified Telecom, Inc.	Demand	
Diversified Telecom, Inc.	5/19/02	1
SECC (formerly MilleCom, Inc.)	3/31/04	9
SECC (formerly MilleCom, Inc.)	5/11/04	3
ISR Solutions, Inc.	6/30/04	7
Fire King International	Demand	5
TABET Manufacturing Co., Inc.	12/31/04	2
National Assisted Living, LP	12/31/04	1,4
Electronic Business Systems, Inc. (formerly Triangle Imaging Group, Inc.) (b)	1/31/05	4
New Dominion Pictures LLC	4/30/06	7
Total debt securities		8,8

8

WATERSIDE CAPITAL CORPORATION

Schedule of Portfolio Investments

June 30, 2000 and December 31, 2000

	Number of shares	Percentage ownership	Cost or contributed value	
Stock Options and Warrants:				
Publicly Traded Companies:				
Avery Communications, Inc.	161,000	0.00	$ -	$
Netplex Group, Inc. (a)	300,000	2.10	900,000	
Electronic Business Systems, Inc. (formerly Triangle Imaging Group, Inc.) (a) (b)	56,000	0.39	-	
Private Companies:				
Real Time Data Management Services, Inc.	125	29.41	115,000	
Delta Education Systems, Inc.	639	39.00	48,200	
Diversified Telecom, Inc.	8,998	15.00	-	
Crispies, Inc.	524	6.37	2,800	
Triangle Biomedical Sciences	50,743	11.70	127,449	
Extraction Technologies of VA, LLC	-	39.00	337,567	
JMS Worldwide, Inc.	199	5.00	-	
EPM Development Systems Corp.	87	8.00	11,600	
Fire King International	4	4.00	-	
SECC (formerly MilleCom, Inc.)	150,000	3.15	-	
Eton Court Asset Management, Ltd.	14,943	13.00	34,700	
Fairfax Publishing Co., Inc.	526	16.50	73,600	
ISR Solutions, Inc.	550,973	7.20	12,936	
DigitalSquare.com	81,074	5.70	-	
Answernet, Inc.	69,837	17.64	268,615	
TABET Manufacturing Co., Inc.	500,000	20.00	175,400	
National Assisted Living, LP	-	15.00	667,000	
Capital Markets Group, Inc.	2,294,118	15.00	-	
Jubilee Tech International, Inc.	400,000	1.60	240,000	
Signius Investment Corporation	12	11.67	332,595	
VentureCom, Inc.	38,943	0.37	-	
New Dominion Pictures LLC	-	9.00	464,650	
Total options and warrants			3,812,112	
Total investments			$ 37,826,396	$

The Company's investment portfolio at December 31, 2000 consisted of the following:

	Number of shares	Cost contrib valu

Equity Securities:		
Publicly Traded Companies:		
Avery Communications, Inc. Common Stock	245,000	$ 2
Avery Communications, Inc. Common Stock (a)	190,167	
Netplex Group, Inc. Common Stock	66,400	4
Netplex Group, Inc. Preferred Stock	1,500,000	1,2
Electronic Business Systems, Inc. (formerly Triangle Imaging Group, Inc.) Convertible Preferred Stock (b) (c)	700	2,0
Electronic Business Systems, Inc. (formerly Triangle Imaging Group, Inc.) Common Stock (b) (c)	500,000	2
Electronic Business Systems, Inc. (formerly Triangle Imaging Group, Inc.) Common Stock (b) (c)	1,423,821	

9

WATERSIDE CAPITAL CORPORATION

Schedule of Portfolio Investments

June 30, 2000 and December 31, 2000

	Number of shares	Cost or contribut value
Private Companies:		
Real Time Data Management Services, Inc. Preferred Stock	300	$ 291
Delta Education Systems, Inc. Preferred Stock	1,625	1,599
Diversified Telecom, Inc. Preferred Stock (c)	1,500	1,500
Crispies, Inc. Preferred Stock	400	398
Triangle Biomedical Sciences Preferred Stock	2,100	2,101
JMS Worldwide, Inc. Preferred Stock	1,500	1,500
EPM Development Systems Corp. Preferred Stock	1,500	1,494
Fire King International Preferred Stock	2,000	2,000
SECC (formerly MilleCom, Inc.) Common Stock	840,000	
Eton Court Asset Management, Ltd. Preferred Stock	1,000	976
Fairfax Publishing Co., Inc. Preferred Stock	1,100	1,190
DigitalSquare.com Convertible Preferred Stock	1,210,739	1,513
Answernet, Inc. Preferred Stock	550	318
Answernet, Inc. Preferred Stock	700	393
ISR Solutions, Inc. Preferred Stock	500	497
Capital Markets Group, Inc. Preferred Stock	1,500	1,500
Jubilee Tech International, Inc. Convertible Preferred Stock	2,200,000	1,988
VentureCom, Inc. Preferred Stock	278,164	2,000
Phoenix Fabrications, Inc. Preferred Stock	400	271
AmeriComm Direct Marketing LLC, Common Stock	27,696	

Total equity securities		25,920

	Maturity	Cost or contribut value
Debt Securities:		
Avery Communications, Inc. Convertible Note	12/10/02	$ 350
Extraction Technologies of VA, LLC (c) (d)	7/22/03	900
Extraction Technologies of VA, LLC (c) (d)	8/31/04	202
Extraction Technologies of VA, LLC (c) (d)	11/2/04	373
Extraction Technologies of VA, LLC (c) (d)	2/7/05	263
Extraction Technologies of VA, LLC (c) (d)	2/25/05	97
Extraction Technologies of VA, LLC (c) (d)	3/14/05	95
JMS Worldwide, Inc.	7/31/03	900
Diversified Telecom, Inc.	Demand	84
Diversified Telecom, Inc.	5/19/02	156
ISR Solutions, Inc.	6/30/04	743
Fire King International	Demand	550
TABET Manufacturing Co., Inc.	12/31/04	293
National Assisted Living, LP	12/31/04	1,489
New Dominion Pictures LLC	4/30/06	758
Mayfair Enterprises, Inc.	7/18/05	493
DigitalSquare.com	9/15/05	289
Phoenix Fabrications, Inc.	9/8/05	339
Kotarides Baking Co. of VA	6/5/01	566
AmeriComm Direct Marketing LLC	12/29/05	750
Total debt securities		9,695

WATERSIDE CAPITAL CORPORATION

Schedule of Portfolio Investments

June 30, 2000 and December 31, 2000

	Number of shares	Percentage ownership	Cost or contribute value
Stock Options and Warrants:			
Publicly Traded Companies:			
Netplex Group, Inc. (a)	300,000	2.10	$ 900,0
Electronic Business Systems, Inc. (formerly Triangle Imaging Group, Inc.) (a) (b)	98,000	0.63	
Private Companies:			
Real Time Data Management Services, Inc.	125	29.41	115,0
Delta Education Systems, Inc.	639	39.00	48,2
Diversified Telecom, Inc.	8,998	15.00	
Crispies, Inc.	524	6.37	2,8
Triangle Biomedical Sciences	50,743	11.70	127,4
Extraction Technologies of VA, LLC (d)	-	39.00	337,5
JMS Worldwide, Inc.	199	5.00	
EPM Development Systems Corp.	87	8.00	11,6
Fire King International	4	4.00	
SECC (formerly MilleCom, Inc.)	150,000	3.15	
Eton Court Asset Management, Ltd.	14,943	13.00	34,7
Fairfax Publishing Co., Inc.	696	15.50	83,6
ISR Solutions, Inc.	588,334	5.90	12,9
DigitalSquare.com	150,000	-	75,0
Answernet, Inc.	69,837	16.50	268,6
TABET Manufacturing Co., Inc.	487,500	19.50	175,4
National Assisted Living, LP	-	15.00	667,0
Capital Markets Group, Inc.	2,294,118	15.00	
Jubilee Tech International, Inc.	400,000	1.60	240,0
Signius Investment Corporation	12	11.67	332,5
VentureCom, Inc.	38,943	0.37	
New Dominion Pictures LLC	-	9.00	464,6
Mayfair Enterprises, Inc.	-	15.00	214,4
Phoenix Fabrications, Inc.	-	25.00	297,0
Kotarides Baking Co. of VA	-	13.75	185,6
Total options and warrants			4,594,1
Total investments			$ 40,209,7

(a) Rule 144A restricted securities.

(b) This entity, which is considered an affiliate of the Company, 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.

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 headquartered 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 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 9 full time employees and 2 offices from which it operates - Norfolk and Reston, Virginia.

. Results of Operations

Comparison of Three Months Ended December 31, 2000 and December 31, 1999

For the three months ended December 31, 2000, total operating income was $939,000 compared to $990,000 reported during the same period of 1999. The decrease in operating income is due to a combination of a reversal of previously accrued interest income of $126,000 associated with the write down of the Extraction Technologies investment and the reduction in fee income due to the origination of fewer investments during the quarter. The December 31, 2000 quarterly operating income consisted of dividends of $646,000, interest on debt securities of $198,000, fee income of $93,000 and interest on cash equivalents of $2,000.

Total operating expenses for the three months ended December 31, 2000, were $834,000, consisting of interest expense of $495,000, salaries and benefits of $205,000, legal and accounting expense of $52,000, and other operating expenses of $82,000. These expenses compared to the $654,000 for the three months ended December 31, 1999, consisting of interest expense of $268,000, salaries and benefits of $211,000, legal and accounting expenses of $50,000, and other operating expenses of $125,000. The significant increase in interest expense for the quarter ended December 31, 2000, compared to the quarter ended December 31, 1999 is due to the increased borrowings made to fund the growth in the company's investment portfolio. Net operating income of $275,000 for the three months ended December 31, 2000, compared to the $393,000 reported for the three months ended December 31, 1999.

12

The realized gain on investments of $986,000 for the three months ended

December 31, 1999 was due to an after tax gain on the company's holdings in the publicly traded investment The Netplex Group. The increase in the change in unrealized appreciation on investments of $1,006,000 for the three months ended December 31, 1999 is primarily attributed to significant increases in the fair values of the company's publicly traded investments. The increase in unrealized depreciation on investments net of taxes of $1,369,000 for the three months ended December 31, 2000 is primarily due to the write down of a portfolio company (Extraction Technologies of Virginia) that filed for bankruptcy protection under Chapter 11 of the U. S. Bankruptcy Code in order to restructure contractual and debt obligations. The remainder of the increase in unrealized depreciation for the three months ended December 31, 2000 is attributable to additional write downs in two publicly traded companies held in the portfolio due to their changing stock prices

The net increase (decrease) in stockholders' equity resulting from operations was a decrease of $1,095,000 or $.69 per share for the quarter ended December 31, 2000, compared to an increase of $2,386,000 or $1.51 per share for the comparable period ended December 31, 1999.

Comparison of Six Months Ended December 31, 2000 and December 31, 1999

For the six months ended December 31, 2000, total operating income was $2,032,000 compared to $1,820,000 reported during the same period of 1999. The increase in operating income is due to the increase in interest and dividend income as a result of the growth in the Company's investment portfolio as compared to 1999 partially offset by the reversal of previously accrued interest income and the reduction in fee income due to the origination of fewer investments during the most recent quarter as described above. The December 31, 2000 year to date operating income consisted of dividends of $1,360,000, interest on debt securities of $459,000, fee income of $205,000 and interest on cash equivalents of $8,000.

Total operating expenses for the six months ended December 31, 2000, were $1,695,000, consisting of interest expense of $958,000, salaries and benefits of $455,000, legal and accounting expense of $95,000, and other operating expenses of $187,000. These expenses compared to the $1,200,000 for the six months ended December 31, 1999, consisting of interest expense of $493,000, salaries and benefits of $429,000, legal and accounting expenses of $74,000, and other operating expenses of $204,000. The significant increase in interest expense for the six months ended December 31, 2000, compared to the six months ended December 31, 1999 is due to the increased borrowings made to fund the growth in the company's investment portfolio. For the six months ended December 31, 2000 net operating income was $656,000 or $.42 per share compared to the $750,000 or $.47 per share reported for the same six month period of the previous fiscal year.

During the six months ended December 31, 1999 Waterside realized a pretax gain of $1.6 million on its holdings in the Netplex group. In addition, it had an increase in pretax unrealized gains on investments of $1.3 million, primarily due to increases in the fair values of its publicly traded investments. Net of taxes, total realized and unrealized gains on investments added $1.8 million to total income during the six months ended December 31, 1999.

During the six months ended December 31, 2000, Waterside recorded pretax unrealized depreciation in the fair value of its investments of $2.4 million, primarily due to the write down of two portfolio companies that each filed for bankruptcy protection under Chapter 11 of the U. S. Bankruptcy Code. The write downs were $1.2 million for Electronic

Business Systems, Inc., and $1.1 million for Extraction Technologies of Virginia. In addition, during the six months ended December 31, 2000 the company reduced its recognized tax benefit by $619,000 on the cumulative unrealized depreciation on investments due to uncertainty as to the realization of these associated tax benefits. The Company will continue to monitor the status of its deferred tax assets to assess whether amounts recognized are more likely than not to be realized.

The net increase (decrease) in stockholders' equity resulting from operations was a decrease of $1,423,000 or $.90 per share for the December 31, 2000 six-month period, compared to an increase of $2,513,000 or $1.59 per share for the comparable period ended December 31, 1999.

. Financial Condition, Liquidity And Capital Resources

At December 31, 2000 the company's investment portfolio totaled $35.9 million compared with the $35.9 million reported at June 30, 2000. For the six months ended December 31, 2000 the company funded $3.8 million in investments compared to the $8.7 million funded during the comparable six months of 1999. To fund these new investments, the company borrowed $3.1 million from the SBA during the six months ended December 31, 2000.

Net asset value per common share decreased to $9.75 per share at December 31, 2000 from $10.65 per share at June 30, 2000. This reduction in net asset value is a result of the investment write downs previously discussed.

During the six months ended December 31, 2000, net cash provided by operating activities was $466,000 as compared to the $215,000 provided during the six months ended December 31, 1999. Refunded income taxes of $323,000 contributed significantly to the cash provided during the six months ended December 31, 2000. The company used $2.1 million in investing activities during the six months ended December 31, 2000 as compared to the $4.5 million used in investing activities for the six months ended December 31, 1999, primarily due to the reduction in investment origination as described above, partially offset by proceeds from sale of investments and repayment of loansCash flows provided by financing activities for the six months ended December 31, 2000 were $1.6 million compared to the $3.7 million provided during the six months ended December 31, 1999, due to increased borrowings in 1999 as compared to 2000 to finance investment origination.

. 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 equity interests 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 twenty-nine investments are in thinly traded, small public companies, whose stock prices have been volatile. The other twenty-six 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 subject to the estimate of 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 equity securities of $35.9 million at December 31, 2000, would have resulted in unrealized gains or losses and would have changed net increase in stockholders' equity resulting from operations for the quarter significantly.

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 affected net increase in stockholders' equity resulting from operations significantly 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 net income. Accordingly, no assurances can be given that actual results would not differ materially from the potential outcome simulated by this estimate.

. 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, 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. 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.

15

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

The 2000 Annual Meeting of Shareholders of Waterside Capital Corporation was held on October 23, 2000 to consider two matters of business. The matters brought before the shareholders and the voting results are as follows:

1. Election of Directors

	FOR	%	WITHHOLD	%
James E. Andrews	1,372,195	99.5	6,834	0.5
J. W. Whiting Chisman, Jr.	1,372,195	99.5	6,834	0.5
Jeffrey R. Ellis	1,372,195	99.5	6,834	0.5
Eric L. Fox	1,372,195	99.5	6,834	0.5
Marvin S. Friedberg	1,372,195	99.5	6,834	0.5
Roger L. Frost	1,372,195	99.5	6,834	0.5
Ernest F. Hardee	1,372,195	99.5	6,834	0.5
Henry U. Harris, III	1,372,195	99.5	6,834	0.5
J. Alan Lindauer	1,372,195	99.5	6,834	0.5
Robert I. Low	1,372,195	99.5	6,834	0.5
Harold J. Marioneaux, Jr.	1,372,195	99.5	6,834	0.5
Peter W. Meredith, Jr.	1,372,195	99.5	6,834	0.5
Charles H. Merriman	1,372,195	99.5	6,834	0.5

Augustus C. Miller	1,372,195	99.5	6,834	0.5
Paul F. Miller	1,372,195	99.5	6,834	0.5
Juan M. Montero	1,372,195	99.5	6,834	0.5
R. Scott Morgan, Sr.	1,372,195	99.5	6,834	0.5
Richard G. Ornstein	1,372,195	99.5	6,834	0.5
Jordan E. Slone	1,372,195	99.5	6,834	0.5

Ratification of the appointment of KPMG LLP as independent auditors for 2001

FOR	%	AGAINST	%	ABSTAIN	%
1,374,517	99.7%	500	0.0%	4,012	0.3%

*"Broker Non-Votes" occur where a broker holding stock in street name does not vote those shares.

ITEM 5. OTHER INFORMATION

In January 2001, the Company entered into employment agreements with four of its executive officers. These agreements provide for a specified annual base salary and certain discretionary bonuses. These agreements expire on January 31, 2004. These amounts provide that if the Company terminates the employee's employment without cause, the Company is obligated to pay the employee an amount equal to two times the employee's base salary as then in effect, plus the average of the bonuses received by the employee for each of the two years prior to the date of termination.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits required by Item 601 of Regulation S-K:

10.1 Employment Agreement, dated as of January 1, 2001, between the Registrant and J. Alan Lindauer.

10.2 Employment Agreement, dated as of January 1, 2001, between the Registrant and Gerald T. McDonald.

10.3 Employment Agreement, dated as of January 1, 2001, between the Registrant and Martin N. Speroni.

10.4 Employment Agreement, dated as of January 1, 2001, between the Registrant and Lex W. Troutman.

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 14th day of February, 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