

ALLIED CAPITAL CORP  
Form 497  
August 22, 2003

Prospectus Supplement  
(To Prospectus dated June 11, 2003)

Filed Pursuant to Rule 497  
Registration Statement No. 333-104149

## 1,000,000 Shares

### Common Stock

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We are offering for sale 1,000,000 shares of our common stock. Our common stock is traded on the New York Stock Exchange under the symbol ALD. The last reported sales price for our common stock on August 21, 2003 was \$24.77 per share.

**You should review the information, including the risk of leverage, set forth under Risk Factors on page 9 of the accompanying prospectus before investing in our common stock.**

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	Per Share	Total
Public offering price	\$24.22	\$24,220,000
Underwriting discount	\$ 1.09	\$ 1,090,000
Proceeds to Allied Capital Corporation(1)	\$23.13	\$23,130,000

(1) Before deducting expenses payable by us estimated to be \$50,000.

Please read this prospectus supplement, and the accompanying prospectus, before investing, and keep it for future reference. The prospectus supplement and the accompanying prospectus contain important information about us. The SEC maintains an Internet website (<http://www.sec.gov>) that contains other information about us.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus supplement or the accompanying prospectus. Any representation to the contrary is a criminal offense.

The shares of common stock will be ready for delivery on or about August 25, 2003.

### Credit Lyonnais Securities (USA) Inc.

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The date of this prospectus supplement is August 21, 2003.

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You should rely only on the information contained in this prospectus supplement and the accompanying prospectus. We have not, and the underwriter has not, authorized any other person to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. We are not, and the underwriter is not, making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. You should assume that the information appearing in this prospectus supplement and the accompanying prospectus is accurate only as of their respective dates. Our business, financial condition, results of operations and prospects may have changed since those dates.

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In this prospectus supplement and the accompanying prospectus, unless otherwise indicated, Allied Capital, we, us or our refer to Allied Capital Corporation and its subsidiaries.

Information contained in this prospectus supplement and the accompanying prospectus may contain forward-looking statements, which can be identified by the use of forward-looking terminology such as may, will, expect, intend, anticipate, estimate, or continue or the negative thereof or other variations thereon or comparable terminology. The matters described in Risk Factors in the accompanying prospectus and certain other factors noted throughout this prospectus supplement and the accompanying prospectus constitute cautionary statements identifying important factors with respect to any such forward-looking statements, including certain risks and uncertainties, that could cause actual results to differ materially from those in such forward-looking statements.

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### FEES AND EXPENSES

This table describes the various costs and expenses that an investor of our common stock will bear directly or indirectly.

<b>Shareholders Transaction Expenses</b>	
Sales load (as a percentage of offering price)(1)	4.5%
Dividend reinvestment plan fees(2)	None
<b>Annual Expenses (as a percentage of consolidated net assets attributable to common shares)(3)</b>	
Operating expenses(4)	3.6%
Interest payments on borrowed funds(5)	4.8%
	<hr/>
Total annual expenses(6)	8.4%
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- (1) Represents the underwriting discounts and commissions with respect to the shares sold by Allied Capital in this offering.
- (2) The expenses of our dividend reinvestment plan are included in Operating expenses. We do not have a stock purchase plan. The participants in the dividend reinvestment plan will bear a pro rata share of brokerage commissions incurred with respect to open market purchases, if any. See Dividend Reinvestment Plan in the accompanying prospectus.
- (3) Consolidated net assets attributable to common stock equals net assets (*i.e.*, total consolidated assets less total consolidated liabilities and preferred stock) at June 30, 2003.
- (4) Operating expenses represent our estimated operating expenses for the year ending December 31, 2003 excluding interest on indebtedness. This percentage for the year ended December 31, 2002 was 3.5%.
- (5) The Interest payments on borrowed funds represents our estimated interest expenses for the year ending December 31, 2003. We had outstanding borrowings of \$979.7 million at June 30, 2003. This percentage for the year ended December 31, 2002 was 4.6%. See Risk Factors in the accompanying prospectus.
- (6) Total annual expenses as a percentage of consolidated net assets attributable to common stock are higher than the total annual expenses percentage would be for a company that is not leveraged. We borrow money to leverage our net assets and increase our total assets. The SEC requires that the Total annual expenses percentage be calculated as a percentage of net assets, rather than the total assets, including assets that have been funded with borrowed monies. If the Total annual expenses percentage were calculated instead as a percentage of consolidated total assets, our Total annual expenses would be 4.9% of consolidated total assets.

#### Example

The following example, required by the SEC, demonstrates the projected dollar amount of total cumulative expenses that would be incurred over various periods with respect to a hypothetical investment in us. In calculating the following expense amounts, we assumed we would have no additional leverage and that our operating expenses would remain at the levels set forth in the table above.

	<u>1 Year</u>	<u>3 Years</u>	<u>5 Years</u>	<u>10 Years</u>
You would pay the following expenses on a \$1,000 investment, assuming a 5.0% annual return	\$127	\$292	\$457	\$870

Although the example assumes (as required by the SEC) a 5.0% annual return, our performance will vary and may result in a return of greater or less than 5.0%. In addition, while the example assumes reinvestment of all dividends and distributions at net asset value, participants in the dividend reinvestment plan may receive shares of common stock that we issue at or above net asset value or purchased by the administrator of the dividend reinvestment plan, at the market price in effect at the time, which may be higher than, at, or below net asset value. See Dividend Reinvestment Plan in the accompanying prospectus.

**The example should not be considered a representation of future expenses, and the actual expenses may be greater or less than those shown.**

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### USE OF PROCEEDS

The net proceeds from the sale of the shares of our common stock, after deducting estimated expenses of this offering, are estimated to be \$23.1 million. We intend to use the net proceeds from selling our common stock for investment in the debt or equity securities of private companies, non-investment grade commercial mortgage-backed securities or collateralized debt obligation bonds and preferred shares and other general corporate purposes.

### UNDERWRITING

Subject to the terms and conditions stated in the underwriting agreement with Credit Lyonnais Securities (USA) Inc., the underwriter has agreed to purchase, and we have agreed to sell to the underwriter, all 1,000,000 of the shares offered by this prospectus supplement.

The underwriting agreement provides that the obligations of the underwriter to purchase the shares offered by us are subject to some conditions. The underwriter is obligated to purchase all of the shares offered by us, if any of the shares are purchased.

The underwriter proposes to offer the shares to the public initially at the public offering price set forth on the cover of this prospectus supplement. The public offering price is equal to the volume weighted average price per share of our common stock on the New York Stock Exchange for each of the twenty trading days beginning on July 25, 2003 and ending on August 21, 2003. After the offering, the public offering price may be changed by the underwriter.

The following table shows the per share and total underwriting discounts and commissions to be paid to the underwriter by us.

Per share	\$ 1.09
Total	\$ 1,090,000

We estimate that the total expenses of this offering, excluding the underwriting discounts and commissions, will be approximately \$50,000, which will be paid by us.

This offering of the shares is made for delivery when, as and if accepted by the underwriter and subject to prior sale and to withdrawal, cancellation or modification of this offering without notice. The underwriter reserves the right to reject an order for the purchase of shares in whole or in part.

We have agreed to indemnify the underwriter against certain liabilities, including liabilities under the Securities Act, and to contribute to payments the underwriter may be required to make in respect of these liabilities.

We have been advised by the underwriter that, in accordance with Regulation M under the Securities Act, some persons participating in this offering may engage in transactions, including syndicate covering transactions or stabilizing bids, that may have the effect of stabilizing or maintaining the market price of the shares at a level above that which might otherwise prevail in the open market.

A syndicate covering transaction is a bid for or the purchase of shares on behalf of the underwriter to reduce a syndicate short position incurred by the underwriter in



connection with this offering. The underwriter may create a syndicate short position by making short sales of our shares and must then purchase our shares in the open market to cover the syndicate short positions created by these short sales. Short sales involve the sale by the underwriter of a greater number of shares than it is required to purchase in this offering. A short position is more likely to be created if the underwriter is concerned that there may be downward pressure in the price of the shares in the open market after pricing that could adversely affect investors who purchase in this offering.

A stabilizing bid is a bid for or the purchase of shares on behalf of the underwriter for the purpose of fixing or maintaining the price of our shares.

We have been advised by the underwriter that these transactions may be effected on the New York Stock Exchange or otherwise and, if commenced, may be discontinued at any time. Similar to other purchase activities, these activities may have the effect of raising or maintaining the market price of our shares or preventing a decline in the market price of our shares. As a result, the price of our shares may be higher than the price that might otherwise exist in the open market.

The underwriter expects to deliver the shares through the facilities of The Depository Trust Company in New York, New York, on or about August 25, 2003. At that time, the underwriter will pay us for the shares in immediately available funds.

In the ordinary course of business, the underwriter and/or its affiliates have in the past performed, and may continue to perform, commercial banking, financial advisory and investment banking services for us for which they have received, or may receive, customary compensation. An affiliate of the underwriter is a member of the lending syndicate for our unsecured revolving line of credit.

The address for Credit Lyonnais Securities (USA) Inc. is 1301 Avenue of the Americas, New York, NY 10019.

#### **LEGAL MATTERS**

Certain legal matters with respect to the validity of the shares of common stock we are offering will be passed upon for us by Sutherland Asbill & Brennan LLP, Washington, D.C. Certain legal matters related to the offering will be passed upon for the underwriter by Morgan, Lewis & Bockius LLP, New York, New York.

**INTERIM MANAGEMENT'S DISCUSSION AND ANALYSIS  
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*The following analysis of our financial condition and results of operations should be read in conjunction with our Consolidated Financial Statements and the Notes thereto included herein and in the accompanying prospectus. The information herein contains certain forward-looking statements. These statements include the plans and objectives of management for future operations and financial objectives and can be identified by the use of forward-looking terminology such as may, will, expect, intend, anticipate, estimate, or continue or the negative thereof or other variations thereon or comparable terminology. These forward-looking statements are subject to the inherent uncertainties in predicting future results and conditions. Certain factors that could cause actual results and conditions to differ materially from those projected in these forward-looking statements are set forth below in the Risk Factors section. Other factors that could cause actual results to differ materially include:*

*the ongoing global economic downturn;*

*risks associated with possible disruption in our operations due to terrorism; and*

*future regulatory actions and conditions in our operating areas.*

*Financial or other information presented for private finance portfolio companies has been obtained from the portfolio company, and the financial information presented may represent unaudited, projected or pro forma financial information, and therefore may not be indicative of actual results. In addition, the private equity industry uses financial measures such as EBITDA or EBITDAM (Earnings Before Interest, Taxes, Depreciation, Amortization and, in some instances, Management fees) in order to assess a portfolio company's financial performance and to value a portfolio company. EBITDA and EBITDAM are not intended to represent cash flow from operations as defined by accounting principles generally accepted in the United States of America and such information should not be considered as an alternative to net income, cash flow from operations or any other measure of performance prescribed by accounting principles generally accepted in the United States of America.*

**OVERVIEW**

We are a business development company that provides long-term debt and equity investment capital to companies in a variety of industries. Our lending and investment activity is generally focused on private finance and commercial real estate finance, primarily the investment in non-investment grade commercial mortgage-backed securities, which we refer to as CMBS, and collateralized debt obligation bonds and preferred shares, which we refer to as CDOs. Our private finance activity principally involves providing financing through privately negotiated long-term debt and equity investment capital. Our private financing is generally used to fund growth, buyouts, acquisitions, recapitalizations, note purchases, and bridge financings. We generally invest in private companies though, from time to time, we may invest in public companies that lack access to public capital or whose securities may not be marginable.

Our portfolio composition at June 30, 2003, and December 31, 2002, was as follows:

	<u>2003</u>	<u>2002</u>
Private Finance	72%	70%
Commercial Real Estate Finance	28%	30%

Our earnings depend primarily on the level of interest and dividend income, fee income, and net gains or losses earned on our investment portfolio after deducting interest paid on borrowed capital and operating expenses. Interest income results from the stated interest rate earned on a loan and the amortization of loan origination points and discounts. The level of interest income is directly related to the balance of the interest-bearing investment portfolio multiplied by the weighted average yield. Our ability to generate interest income is dependent on economic, regulatory, and competitive factors that influence new investment activity, the amount of loans and debt securities for which interest is not accruing and our ability to secure debt and equity capital for our investment activities.

## PORTFOLIO AND INVESTMENT ACTIVITY

Total portfolio investment activity and yields at and for the three and six months ended June 30, 2003 and 2002, and at and for the year ended December 31, 2002, were as follows:

(\$ in millions)	At and for the Three Months Ended June 30,		At and for the Six Months Ended June 30,		At and for the Year Ended December 31,
	2003	2002	2003	2002	2002
	(unaudited)		(unaudited)		
Portfolio at value	\$ 2,546.1	\$ 2,381.0	\$ 2,546.1	\$ 2,381.0	\$ 2,488.2
Investments funded	\$ 257.4	\$ 115.5	\$ 526.4	\$ 195.5	\$ 506.4
Change in accrued or reinvested interest and dividends	\$ 9.3	\$ 6.2	\$ 20.4	\$ 19.5	\$ 44.7
Principal repayments	\$ 74.3	\$ 36.0	\$ 150.3	\$ 67.0	\$ 143.2
Sales	\$ 32.6	\$ 1.2	\$ 276.7	\$ 126.3	\$ 213.5
Yield <sup>(1)</sup>	14.1%	13.8%	14.1%	13.8%	14.0%

(1) The weighted average yield on interest-bearing investments is computed as the (a) annual stated interest rate earned plus the annual amortization of loan origination fees, original issue discount, and market discount earned on accruing interest-bearing investments, divided by (b) total interest-bearing investments at value. The weighted average yield is computed as of the balance sheet date.

## Private Finance

The private finance portfolio, investment activity, and yields at and for the three and six months ended June 30, 2003 and 2002, and at and for the year ended December 31, 2002, were as follows:

(\$ in millions)	At and for the Three Months Ended June 30,		At and for the Six Months Ended June 30,		At and for the Year Ended December 31,
	2003	2002	2003	2002	2002
	(unaudited)		(unaudited)		
Portfolio at value:					
Loans and debt securities	\$ 1,192.4	\$ 1,050.8	\$ 1,192.4	\$ 1,050.8	\$ 1,151.2
Equity interests	646.8	584.5	646.8	584.5	592.0
Total portfolio	\$ 1,839.2	\$ 1,635.3	\$ 1,839.2	\$ 1,635.3	\$ 1,743.2
Investments funded	\$ 163.8	\$ 32.2	\$ 273.9	\$ 69.8	\$ 297.2
Change in accrued or reinvested interest and dividends	\$ 8.1	\$ 7.0	\$ 19.4	\$ 19.1	\$ 42.6
Principal repayments	\$ 70.9	\$ 27.2	\$ 146.0	\$ 56.0	\$ 129.3
Yield <sup>(1)</sup>	14.4%	13.9%	14.4%	13.9%	14.4%

(1) The weighted average yield on loans and debt securities is computed as the (a) annual stated interest rate earned plus the annual amortization of loan origination fees, original issue discount, and market discount earned on accruing loans and debt securities, divided by (b) total loans and debt securities at value. The weighted average yield is computed as of the balance sheet date.



Investments funded for the six months ended June 30, 2003 and 2002, and for the year ended December 31, 2002, consisted of the following:

(\$ in millions)	Loans and Debt Securities	Equity Interests	Total
<b><i>For the Six Months Ended June 30, 2003<sup>(1)</sup></i></b>			
Companies more than 25% owned	\$ 42.2	\$ 25.2	\$ 67.4
Companies 5% to 25% owned	9.5	1.0	10.5
Companies less than 5% owned	190.6	5.4	196.0
Total	\$ 242.3	\$ 31.6	\$ 273.9
<b><i>For the Six Months Ended June 30, 2002<sup>(1)</sup></i></b>			
Companies more than 25% owned	\$ 16.0	\$ 3.8	\$ 19.8
Companies 5% to 25% owned	7.5	7.0	14.5
Companies less than 5% owned	34.0	1.5	35.5
Total	\$ 57.5	\$ 12.3	\$ 69.8
<b><i>For the Year Ended December 31, 2002<sup>(1)</sup></i></b>			
Companies more than 25% owned	\$ 86.1	\$ 18.7	\$ 104.8
Companies 5% to 25% owned	22.3	0.4	22.7
Companies less than 5% owned	154.6	15.1	169.7
Total	\$ 263.0	\$ 34.2	\$ 297.2

- (1) The private finance portfolio is presented in three categories – companies more than 25% owned, which represent portfolio companies where we directly or indirectly own more than 25% of the outstanding voting securities of such portfolio company and, therefore, are deemed controlled by us under the Investment Company Act of 1940, or the 1940 Act; companies owned 5% to 25%, which represent portfolio companies where we directly or indirectly own 5% to 25% of the outstanding voting securities of such portfolio company or where we hold one or more seats on the portfolio company’s board of directors and, therefore, are deemed to be an affiliated person under the 1940 Act; and companies less than 5% owned, which represent portfolio companies where we directly or indirectly own less than 5% of the outstanding voting securities of such portfolio company and where we have no other affiliations with such portfolio company.

At June 30, 2003, we had outstanding funding commitments of \$103.9 million to portfolio companies, including \$27.4 million committed to private venture capital funds. At June 30, 2003, we also had total commitments to portfolio companies in the form of standby letters of credit and guarantees of \$96.0 million.

We fund new investments using cash, through the issuance of our common equity, the reinvestment of previously accrued interest and dividends in debt or equity securities, or the current reinvestment of interest and dividend income through the receipt of a debt or equity security (payment-in-kind income). From time to time we may opt to reinvest accrued interest receivable in a new debt or equity security in lieu of receiving such interest in cash and providing a subsequent investment.

We may acquire more than 50% of the common stock of a company in a control buyout transaction. Control investments are generally structured such that we earn a current return through a combination of interest income on our senior loans and subordinated debt, dividends on our preferred and common stock, and management or transaction services fees to compensate us for the managerial assistance that we provide to a controlled portfolio company. We plan to continue to seek attractive control investments.

Control investments provide the opportunity to invest meaningful amounts of capital with the potential for attractive current income returns as well as the potential for future capital gains. Control transactions are typically larger than our mezzanine investments. In some cases for companies that are more than 50% owned, we may not accrue interest on loans and debt securities if such company is in need of additional working capital. In such cases, we may defer current debt service. Our most significant investments acquired through control buyout transactions at June 30, 2003, were Business Loan Express, LLC (BLX), acquired in 2000, and The Hillman Companies, Inc., acquired in 2001.

**Business Loan Express, LLC.** At June 30, 2003, our investment in BLX totaled \$264.7 million at cost and \$356.8 million at value, or 12.6% of our total assets, which includes unrealized appreciation of \$92.1 million.

BLX is the nation's second largest non-bank, government guaranteed lender utilizing the SBA's 7(a) Guaranteed Loan Program and is licensed by the SBA as a Small Business Lending Company (SBLC). BLX is a preferred lender as designated by the SBA, and originates, sells, and services small business loans. In addition to the SBA 7(a) Guaranteed Loan Program, BLX originates conventional small business loans and originates loans under the USDA Business and Industry Guaranteed Loan Program. BLX has offices across the United States and is headquartered in New York, New York. Changes in the laws or regulations that govern SBLCs or the SBA 7(a) Guaranteed Loan Program or changes in government funding for this program could have a material adverse impact on BLX and, as a result, negatively affect our financial results.

During the quarter ended March 31, 2003, BLX completed two significant transactions, the purchase of loans and other assets from Amresco Independence Funding, Inc., or AIF, and the reorganization of BLX from a corporation to a limited liability company, or LLC.

In January 2003, BLX completed the acquisition of \$128.0 million of performing loans and other assets from AIF. BLX purchased \$121.5 million of performing SBA 7(a) unguaranteed loans at par and \$6.5 million of other assets. The acquisition increased BLX's serviced portfolio and enhanced its nationwide loan origination platform. We provided \$50 million of the capital to fund this acquisition. Our \$50 million financing was in the form of a short-term revolving credit facility of \$25 million to fund the temporary capital needs of construction loans purchased and loans pending sale, as well as \$25 million of preferred equity to support the future growth potential of BLX post acquisition.

In February 2003, BLX completed a reorganization from a corporation to a limited liability company in order to simplify its corporate structure and provide certain income tax efficiencies. In connection with the reorganization, BLX's stated book equity increased by \$43 million because we converted \$43 million of our subordinated debt into preferred stock in BLX, Inc., which was exchanged for Class A equity interests in BLX, LLC. In addition, we exchanged our existing preferred stock and common equity investments in BLX, Inc. for similar classes of members' equity in BLX, LLC represented by Class B and Class C equity interests, respectively.

Subsequent to the reorganization, BLX's taxable earnings will flow directly to its members and we represent approximately 95% of the economic interests in the LLC. In connection with the reorganization, BLX has changed its fiscal year end to September 30.

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Summary financial data for BLX at and for the twelve months ended June 30, 2003 and 2002, is presented below.

(\$ in millions)	For the Twelve Months Ended June 30, 2003 <sup>(1)</sup>	For the Twelve Months Ended June 30, 2002
<b>Operating Data</b>		
Total revenue	\$ 109.1	\$ 84.6
Net income <sup>(4)</sup>	\$ 7.5	\$ 2.3
Earnings before interest, taxes and management fees (EBITM) <sup>(4)</sup>	\$ 44.4	\$ 43.0
<b>Balance Sheet Data</b>		
Total assets <sup>(2)</sup>	\$ 340.0	\$ 277.1
Total debt	\$ 166.0	\$ 183.0
Total owners' equity	\$ 137.0	\$ 59.9
<b>Other Data</b>		
Total loan originations	\$ 718.1	\$ 565.1
Serviced loan portfolio	\$2,165.5	\$1,372.6
Number of loans	3,048	2,083
Loan delinquencies <sup>(3)</sup>	8.1%	9.4%
<b>Serviced Loan Portfolio by Industry</b>		
Hotels	24%	27%
Gas stations/convenience stores	18	16
Professional and retail services	12	10
Restaurants	9	10
Manufacturing and industrial	9	10
Car wash/auto repair services	7	3
Child care and health care services	6	4
Shrimp/fishing vessels	5	7
Recreation	5	5
Other	5	8
Total	100%	100%

(1) Post reorganization BLX's fiscal year end changed to September 30. The results of operations and loan originations for the twelve months ended June 30, 2003, are not necessarily indicative of the operating results to be expected for the fiscal twelve months ending September 30, 2003.

(2) Included in total assets is \$6 million of goodwill at June 30, 2003 and 2002. There is no other goodwill on BLX's balance sheet. We acquired 94.9% of BLC Financial Services, Inc. on Dece