Equus Total Return Fund; An Opportunity To Unlock Value

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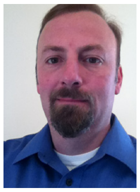

Equus Total Return Fund has been on the rocks for many years, now it trades at dramatic discounts to it NAV and offers shareholders an opportunity to unlock value.

What To Do With Equus Total Return Fund

The Equus Total Return Fund is a very small BDC with change on the horizon. Before I go on I want to take a quick look at Equus Total Return Fund and what they do. The fund operates in 5 segments through wholly owned subsidiaries and equity stakes. The worst performing asset, Equus Media Development Co LLC, a wholly owned subsidiary, is in business to purchase and develop media assets including but not limited to motion pictures. The initial investment was $3 million dollar but is now valued at only $215,000, representing about 10% of currently carried capital losses.

Equus Energy is another wholly owned subsidiary created for the purpose of investing in the energy industry. It was begun with two investment, in 2011 and 2012, totaling more than $7 million and now valued at only $4.5 million. The

decreased valuation is due primarily to lower forward prices for oil and gas used to determine the fair value of the holdings. Holdings consist of 130 operational and non-operational wells and more than 21,000 acres spread across Texas and Oklahoma including oil and shale holdings in the Eagleford Basin. Operational wells are leased to producers such as Chevron which operates about half.

Another investment, but one with much better prospects, is an 18.8% equity stake in Pallet One. Pallet One is the nations largest manufacturer of wooden shipping pallets. The company is headquartered in Florida with operations throughout eastern USA and represents about 40% of assets held. The good news is that Pallet One's revenue and earnings have been on the rise in recent quarters. As of the latest reporting Pallet One says TTM revenue and earnings are significantly higher than in previous periods resulting in a 20.8% increase in valuation which equates to a $2 million gain for Equus, from $9.6 million to $11.6 million. In the previous quarter Pallet

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One's valuation was also increased by $2 million, from $7.6 million, and has nearly doubled in value over the past 6 months.

Equus also has a debt investment in 5th Element Tracking, a technology holding company, headquartered in Texas. Equus issued $915,000 in promissory notes due January of this year. 5th Element is focused on technology to assist in security and the recovery of stolen goods, there is little news on the status of the investment. A similar investment was made in a company called Biogenic Reagents, a company producing high value carbon products for metallurgy and filters. The notes were due May 31st, a payment of $40,000 was received in April.

The fifth segment of business is an equity stake in MVC Capital. MVC is a BDC as well, the deal involved exchange of equity shares between the two companies. Equus delivered 415,946 shares for a 1.8% interest in MVC at a cost of $5,815,000. Since the initial investment Equus has received an additional 12,716 shares in the form of dividend payment. The bad news is that in the time since the initial investment was made the entire BDC complex has been plagued by bearish sentiment resulting in a near 50% decline in value for Equus. As of last report the MVC stake was valued at only $3.2 million.

Under the terms of the share exchange with MVC, and material to EQS ability to operate as a BDC under the Investment Company Act of 1940, the company must effect a merger with MVC, one of its subsidiaries or portfolio companies. This is yet to occur and leaves EQS with three options. The first is to complete the merger, the second is to terminate and the third is to restructure in a different way. The risk is that, if the merger is terminated, that EQS will be forced to repurchase its shares from MVC which owns about 35% of the company.

Valuation And The Future Of Equus Total Return Fund

The Equus Fund is currently valued at roughly $37.6 million, up about $0.3 million from the previous quarter and up 6% from last year at this same time. On a per share basis this comes out to $2.96, a gain of $0.02 from the previous quarter. With shares trading near $1.75 this provides a whopping 58% discount for investors. Obviously there is reason for this discount but that does not mean there is not value to be had. I think it goes without saying that the investment strategy is a little erratic and without focus. In my opinion a break-up or sell-off of some assets may be the best thing the company could do. Simply based on NAV and current share value there is quite a lot of value in the portfolio, for the right buyers.

For starters let's take a look at the media company. It is obviously not performing and the first thing that should be sold. I'm sure whatever assets are left would be of interest to a better positioned media company, the sale of which would raise capital for reinvestment and curb further losses. With this done the next step may be to reduce exposure to the energy sector. With oil prices trading at 10 month highs rigs and acreage could be sold, raising capital and reducing annual losses currently attributable to them.

This would leave two debt investments (5th Element and Biogenic Reagents), Pallet One and MVC Capital. The debt investments will eventually be repaid, or written off, leaving only Pallet One and MVC Capital. Pallet One may be the best thing about the Equus Total Return Fund since it is the only investment currently performing in a positive fashion. An additional investment in this company could help it grow and further gains in revenue, earnings and valuation made over the past 6 months.

Finally, MVC Capital. This investment poses as much a problem for them as it does for Equus and bears close watching. This merger was initially intended to go through 2 years ago but has been hindered by accounting issues at EQS as well as deteriorating conditions in the BDC market. According to 10K filings management "expects to commence and/or consummate a merger" sometime this year. MVC is already the largest shareholder of EQS, about 35%, followed by board member Bertrand des Pallierres who owns about 16%.

Something Is Happening, What Is The Question

The bottom line is this. Equus is a very small and ailing BDC company but one that still has value. It is unlikely it can continue on as it has but there are some possibilities, namely a liquidation of assets or a completion of the merger with MVC. With shares trading at such a low valuation it almost begs to be owned, a total liquidation of the portfolio could provide as much as 69% in total returns for new shareholders if NAV is realize. . .the caveat being the sale of some or all of the assets not guaranteed. However, purchases of shares, 220,641 to be exact, over the past 6 months by board members Bertrand des Pallierres and Robert C. Knauss certainly seem to point to something happening this year.