

Holding the lead

First-quarter life sciences venture capital investment rises year over year but declines from previous period; sector still captures largest share of funding

April 2010



Venture capital funding for the life sciences sector¹ rose year over year during the first quarter of 2010 but declined from the previous quarter, according to findings from the MoneyTree™ Report by PricewaterhouseCoopers and the National Venture Capital Association (NVCA), based on data from Thomson Reuters. For all industries, US venture capitalists invested \$4.7 billion in 681 deals during the first quarter of 2010. Life sciences again captured the largest share at \$1.3 billion in 160 deals, but sector investment was down 26 percent in dollars and 21 percent in deals from the last quarter of 2009.

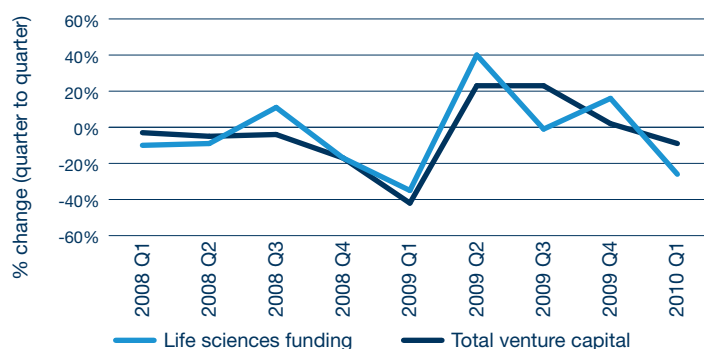
“Life sciences continues to be the No. 1 sector for venture capital investing, with biotechnology being the absolute single-industry leader in dollars invested over the past four quarters,” noted Tracy T. Lefteroff, global managing partner of the venture capital practice at PricewaterhouseCoopers. “Venture capitalists continue to exhibit great confidence in the life sciences sector, as well as clean technology, as they outperformed all others in venture capital investing in the first quarter. Venture capitalists are upholding the belief that the prospects for liquidity are good in these areas, and we continue to see IPO [initial public offering] filings for venture-capital-backed companies in each of these sectors.”

Standing out in terms of improvement during this first quarter, investment in clean technology jumped 87 percent in dollars (to \$773 million) and 44 percent in deals (to 69) from the fourth quarter of 2009. Clean technology crosses traditional MoneyTree industries and comprises alternative energy, pollution control and recycling, power supplies, and conservation. Energy was the only typically leading sector to see an increase in funding during the first quarter.

This quarter marked a period of slow economic recovery and political uncertainty for the life sciences sector. “It’s too early to say that the first-quarter decline in sector funding represents a trend,” said Lefteroff. “A drop in first-quarter funding is not unusual. Looking back, we see that funding has declined in the first quarter as compared to the prior quarter in 10 out of 15 years. Funding activity typically increases in the fourth quarter when venture capital firms try to meet their investment allocation targets.”

The sector is off to a better start in 2010 than in 2009, a year that marked the lowest level of dollar investment since 1997.

Figure 1: Life sciences funding compared with total venture funding



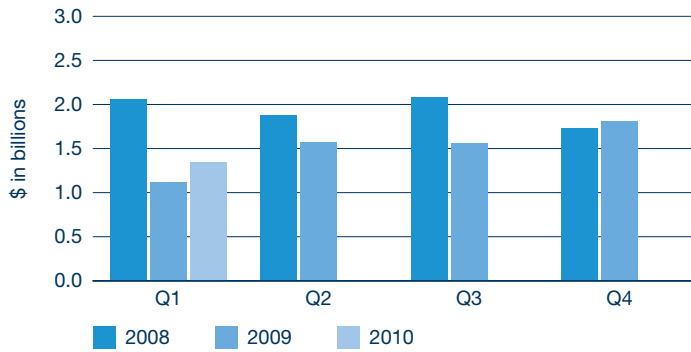
Life sciences funding by quarter

Compared to the first quarter of 2009, life sciences investment grew by 20 percent in the first quarter of 2010. It dropped 26 percent, however, from the last quarter of 2009.

Life sciences was one of eight of the 17 MoneyTree sectors experiencing dollar declines during the first quarter of 2010. Seeing steeper drops were media and entertainment at 29 percent and networking and equipment at 53 percent.

¹ The MoneyTree life sciences sector includes the biotechnology and medical device and equipment industries. *Biotechnology* is defined as “developers of technology promoting drug development, disease treatment, and a deeper understanding of living organisms; includes human, animal, and industrial biotechnology products and services. Also included are biosensors, biotechnology equipment, and pharmaceuticals.” *Medical devices and equipment industries* are defined as those that “manufacture and/or sell medical instruments and devices including medical diagnostic equipment (X-ray, CAT scan, MRI), medical therapeutic devices (drug delivery, surgical instruments, pacemakers, artificial organs), and other health-related products such as medical monitoring equipment, handicap aids, reading glasses, and contact lenses.”

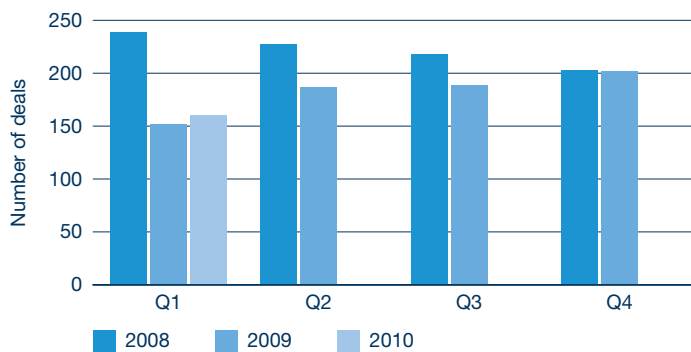
Figure 2: Life sciences funding trends by quarter 2008–2010



Life sciences deal volume by quarter

Compared to the first quarter of 2009, deal volume increased by 5 percent in the first quarter of 2010 to 160. The volume decreased 21 percent, however, from the last quarter of 2009. The most recent quarter reversed an upward trend in deal activity, which had grown for three previous quarters.

Figure 3: Life sciences deal volume by quarter 2008–2010

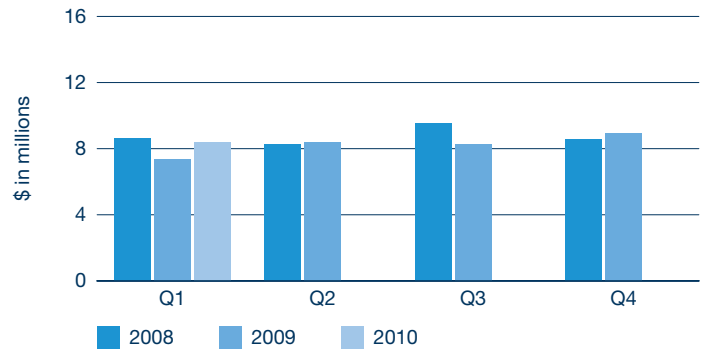


Life sciences average deal size by quarter

Average deal size has remained relatively stable during the past few years. Deal size for the first quarter of 2010 increased by 14 percent compared to last year's first quarter.

The biotechnology industry captured two of the top 10 venture capital deals for the quarter, gaining \$51 million in start-up/seed investment for a biopharmaceutical company and \$47.8 million in expansion funding for a company that develops renewable hydrocarbon biofuels.

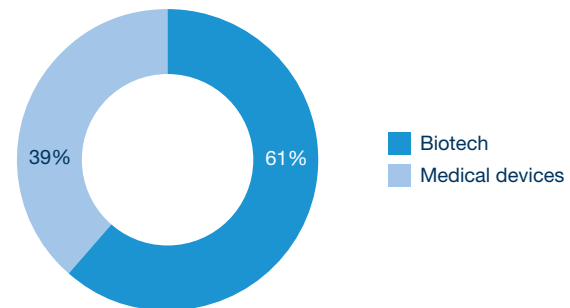
Figure 4: Life sciences average deal size by quarter 2008–2010



Funding for biotechnology and medical devices

The life sciences sector's investment split for the first quarter of 2010 remained consistent with previous years. Biotechnology accounted for 61 percent, while medical devices claimed 39 percent. In comparison, during the first quarter of 2009 biotechnology captured 56 percent of investment in the sector.

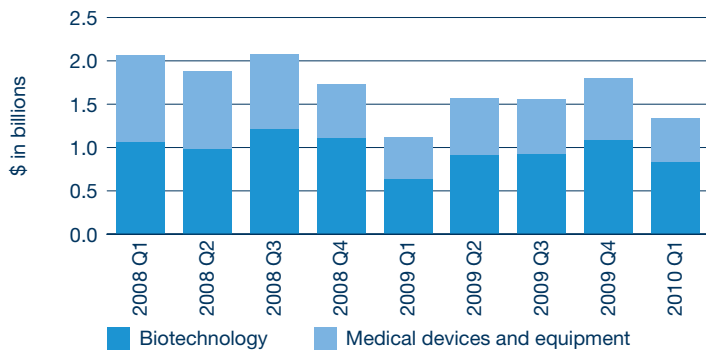
Figure 5: Life sciences investment split for the first quarter of 2010



Despite capturing the largest share of venture capital of any industry during the first quarter of 2010, biotechnology dropped to \$825 million in 99 deals from \$1 billion in 115 deals for the final quarter of 2009. The drop represented a 24 percent decrease in dollars and 14 percent decrease in deals. Compared to the first quarter of last year, however, biotechnology funding was off to a better start, showing a 31 percent year-over-year rise.

The medical device industry showed a smaller year-over-year increase of 6 percent in dollars invested but a similar decline of 29 percent from the previous quarter. Medical devices ranked fourth for the quarter in overall venture capital investment, with \$517 million going into 61 deals.

Figure 6: Biotechnology and medical devices funding trends 2008–2010

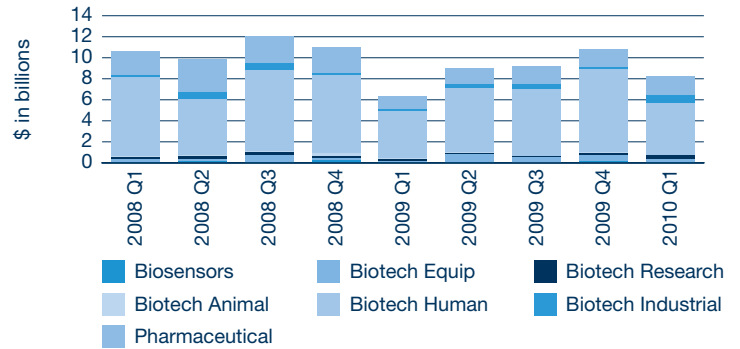


Biotechnology funding by subsegment

Although declining from the last quarter of 2009, all but one biotechnology subsegment, when compared to the same time last year, showed investment growth. Animal biotechnology was the lone subsegment not to grow year over year, with zero funding for the first quarter of 2010.

Two subsegments boosted their funding from the previous quarter. Industrial biotechnology grew from \$22 million in the last quarter of 2009 to \$81 million in the first quarter of 2010. Additionally, biotechnology research grew from \$19 million to \$34 million during the most recent quarter. Average deal size was higher for the areas that saw funding increase. Investment in the biotech pharmaceutical subsegment remained stable.

Figure 7: Biotechnology funding by subsegment 2008–2010

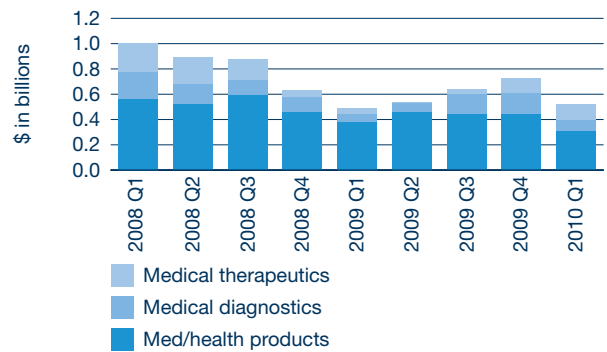


Medical device funding by subsegment

Funding for the medical device subsegments dropped from the previous quarter with the exception of medical/health products, which improved year over year and quarter over quarter.

Funding for the medical diagnostics subsegment declined by 45 percent from the previous quarter but rose 53 percent year over year. On the other hand, the medical therapeutics subsegment declined sequentially (by 31 percent) as well as year over year (by 20 percent).

Figure 8: Medical devices and equipment funding by subsegment 2008–2010

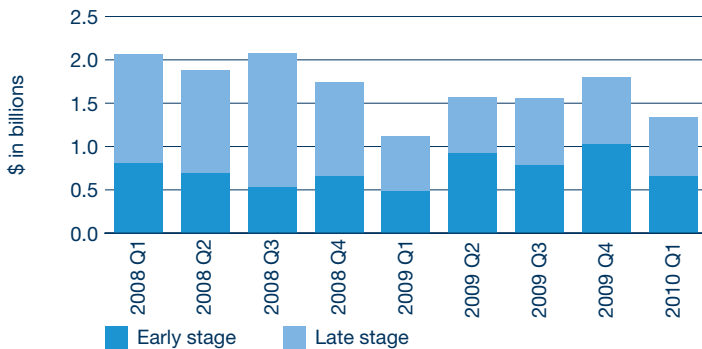


The drug delivery technology area of medical therapeutics received \$129 million in funding during the first quarter of 2010. Surgical instrumentation and pacemakers received \$67 million and \$46 million, respectively.

Life sciences funding by stage

Both early- and late-stage funding decreased in terms of dollars from the previous quarter but rose year over year. Late-stage funding increased by 8 percent compared to the same quarter of 2009 but decreased by 11 percent compared to the fourth quarter of last year. Early-stage funding increased by 35 percent compared to the first quarter a year ago yet decreased by 36 percent from the last quarter of 2009. Early-stage deal volume also declined from the last quarter of 2009 to the first quarter of 2010.

Figure 9: Life sciences funding by stage 2008–2010

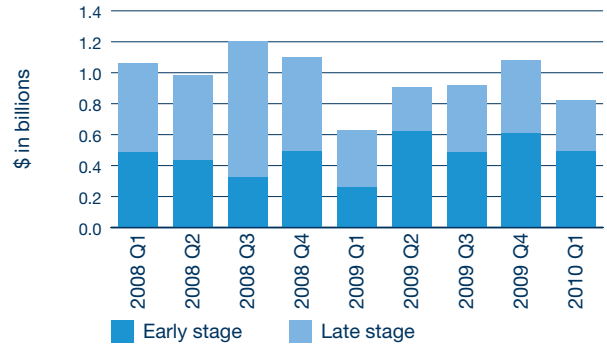


Biotechnology funding by stage

Early-stage biotechnology investment outpaced late-stage, continuing a four-quarter trend. Early-stage funding leaped by 91 percent over the same period of 2009. In contrast, late-stage declined by 11 percent year over year. Both stages fell from the previous quarter.

“It’s not surprising that more venture capital continues to go to early-stage companies,” Lefteroff commented. “Later-stage biotechs are less dependent on venture financing. They have greater exit opportunities, such as IPOs, partnerships, and licensing agreements. Companies farther along in the development process also are more likely to be acquired by or merge with others.”

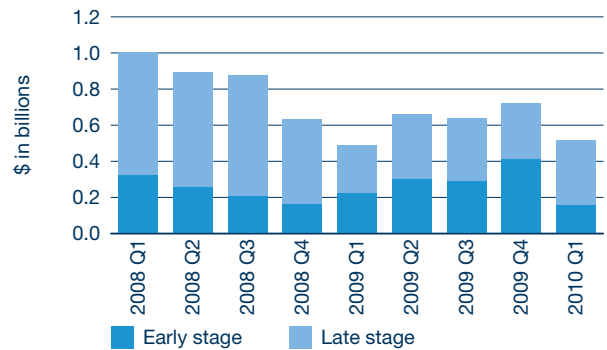
Figure 10: Biotechnology funding by stage 2008–2010



Medical device funding by stage

For the medical device industry, late-stage funding fared better. Compared to the same period of last year, early-stage funding dropped by 30 percent, while late-stage grew by 36 percent. Both stages declined from the last quarter of 2009, with early-stage dropping by 62 percent. Although overall medical device investment rose slightly compared to the first quarter of last year, the industry struggles to regain the higher levels of 2008.

Figure 11: Medical device funding by stage 2008–2010

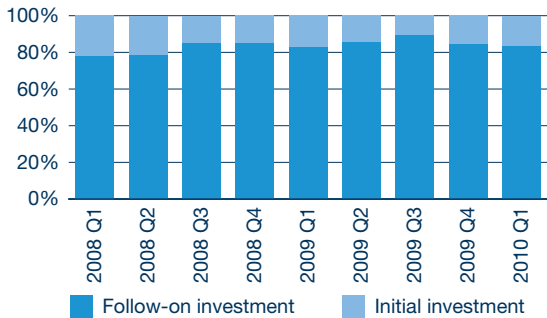


First-time funding compared to follow-on funding

Follow-on continued to outpace first-time financing for the life sciences sector. In the first quarter of 2010, only \$225 million went to initial investments, whereas follow-on funding captured \$1.1 billion. “This disparity has exacerbated the difficulty start-ups have experienced in raising capital throughout the recession,” Lefteroff noted.

Following the overall sector trend, both first-time and follow-on funding increased compared to the first quarter of 2009 but declined from the last quarter. First-time deals in the life sciences sector averaged \$5.8 million during the first quarter of 2010.

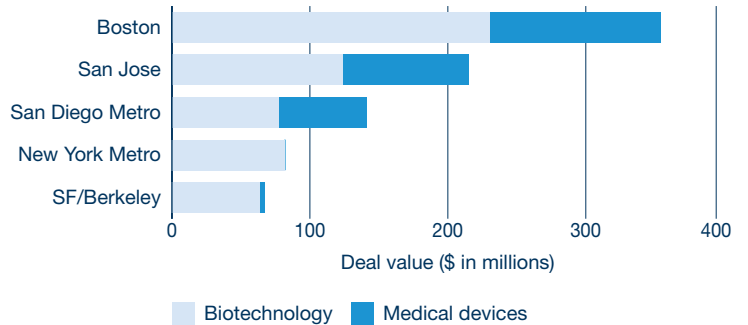
Figure 12: Life sciences follow-on compared to initial investments 2008–2010



Regional funding trends

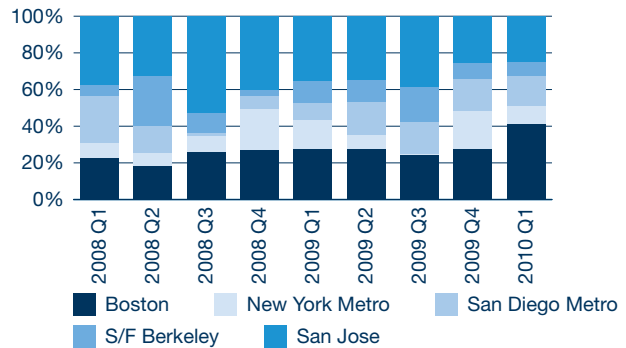
Boston, San Jose, San Diego Metro, New York Metro, and San Francisco-Berkeley received the most life sciences venture capital dollars during the first quarter of 2010. Boston gained \$354 million, with \$230 million going into biotechnology.

Figure 13: Top five metropolitan regions 2008–2010



Funding trends for the top five regions showed an increase in funding for Boston, which grew from \$306 million in the last quarter of 2009. Conversely, New York Metro region investment declined significantly from \$226 million in the last quarter of 2009 to \$81 million in the first quarter of 2010. San Jose, San Diego, and San Francisco-Berkeley investment also decreased from the last quarter of 2009.

Figure 14: Funding trends in top five regions 2008–2010



Venture capital outlook

The venture capital organization expects many venture firms to focus on fundraising this year. “We still anticipate investment levels to mirror that of the mid-1990s,” said Mark Heesen, NVCA president, noting that investment should “increase moderately throughout the rest of 2010.”

US venture capital firms experienced the slowest opening quarter since 1993, raising \$3.6 billion from 32 funds, according to Thomson Reuters and the NVCA. This level represents a 31 percent decline in dollar commitments compared to the first quarter of 2009 and a 44 percent drop in the number of funds. The NVCA expects to see more industry consolidation over the next few years.²

On a positive note, venture-backed company exit activity improved during the first quarter of 2010, with the

best quarterly total for venture-backed IPOs since the fourth quarter of 2007 and the best quarter on record for venture-backed merger and acquisition (M&A) exits, according to the Exit Poll report by Thomson Reuters and the NVCA.³

Although M&A activity was slow for the life sciences sector during the first quarter, the biotechnology sector claimed three of the nine IPOs for the quarter and the largest venture-backed IPO exit at \$187.5 million.⁴

Lefteroff predicted that the life sciences sector will continue to attract the largest share of US venture capital investment. “The demand for innovative pharmaceuticals, diagnostics, and devices will continue to grow,” he said, “as medical care becomes more targeted, personalized, and outcomes focused.”

² “Venture Capital Fundraising Experiences a Slow Start to 2010,” Thomson Reuters and National Venture Capital Association news release, April 12, 2010.

³ “Venture-backed Exit Activity Shows Improved Signs of Life in Q1 2010,” Thomson Reuters and National Venture Capital Association news release, April 1, 2010.

⁴ Ibid.

About PricewaterhouseCoopers' Pharmaceutical and Life Sciences Industry Group

PricewaterhouseCoopers' Pharmaceutical and Life Sciences Industry Group (www.pwc.com/medtech) is dedicated to delivering effective solutions to the complex strategic, operational, and financial challenges facing medical device companies. We provide industry-focused assurance, tax, and advisory services to build public trust and enhance value for our clients and their stakeholders. More than 163,000 people in 151 countries across our network share their thinking, experience, and solutions to develop fresh perspectives and practical advice.

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