VCs want to have their cake and eat it too

Mass Device

The new mantra of the venture capitalist is capital efficiency.

I must have heard that six or seven times while attending the IN3 investor's conference [1] in Boston this week. The event, put on by Elsevier Business Intelligence, brings together startups, established companies and venture capitalists; three interdependent partners with competing interests. After all, the startups want to get the VCs' money, who don't want to give it to them. The VCs want to sell their companies to the big companies, who don't want to give them the valuations they want. And everyone wants to sell their company to Boston Scientific Corp. (NYSE:BSX) or Covidien plc (NYSE:COV).

But in the world of the still-thawing capital markets and slushy IPO market, more than ever venture capitalists have caught the austerity bug. Austerity and VCs? What's next, they'll start wearing ties?

At the heart of the matter, there remains a massive bottleneck of investments venture firms made in med-tech startups during the boom years, anticipating exits through IPOs and mergers in relatively short time frames. But without traditional exits and limited buyers, that model seems to have lost its luster, leaving many VCs wondering if we're at the bottom — or even more frightening, whether we still have farther to fall.

"We haven't hit the bottom yet," Paul LaViolette, a venture partner at SV Life Sciences [2] told the group. "There's a whole pipeline of companies that still have to fail before we have market equilibrium."

The buyers there are are being "prudent," looking for the best deals for bolt-on acquisitions but only at the right price, LaViolette added.

"They're waiting you out," he said.

But don't count LaViolette, who spent more than 15 years in various executive roles at Boston Scientific, as a naysayer: "The long-term market is very attractive, but the short term is going to be very tough."

So how does this trickle down to entrepreneurs? Almost every presenting venture firm at the conference said they're looking for companies who can last longer on fewer resources, or be "capital efficient," a polite way of saying "Don't waste our money, Jack."

Furthermore, VCs are saying they want companies to boot-strap longer and come to them with a clear pathway through the regulatory pipeline — or even, in

some cases, having already passed through it. But don't for a second think that this new reality has many venture firms believing that the days of home runs are over. They're still looking for big exits within three to four years, which likely means even fewer early-round investments.

"There's not a lot of reward for firms that come in early in the process," said Dan Galles of HLM Venture Partners [3], pointing out that companies on the acquiring end are looking for more than great technology: They want market penetration.

A point made perhaps more eloquently by Tom Robinson, the vice president of business development at Boston Scientific, who said that the days of using "large patient pool multiplied by a high price" to prove market adoption is over.

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