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OUTCOME CAPITAL

Attracting venture capital in the life sciences industry: a data-driven approach

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Seeking venture capital (VC) financing for a young life sciences company is often a difficult and frustrating job, sometimes taking many months and too often ending fruitlessly.

Thus it pays to consider the external factors that influence a successful equity financing and take a data-driven approach before embarking on such a quest. Management teams should make every effort to gather as much data on relevant venture financings as possible, analyze that data, and devise a financing strategy that aligns with prevailing market dynamics.

An evidence-based, focused and targeted outreach, as opposed to an indiscriminate blanket approach, is likely to not only be more productive, but also save significant management time and capital.

Moreover, as the venture community is both relatively small and close knit (many venture groups engage in routine discussions with one another), a targeted approach allows a company to maintain control of its financing process and prevents "tainting" the market by having one venture group pass on the opportunity and influence other venture groups to do likewise.

Below are a few questions management teams would do well to consider to build their venture financing data set; similarly, the respective significance of each data point is also shared:

- How many financings in your sector have occurred in the past eight quarters? How does this compare with other sectors?

Significance: multiple rounds of financing in your sector confirm investors' interest and flow of capital into your space. Lack of investment activity suggests an up-hill battle to generate interest.

- At what stage (pre-clinical, Phase I, CE-Mark, etc) were the targets of those financings?

Significance: The venture community rewards companies that possess not only a strong value proposition, but also demonstrate a compelling argument as to de-risking milestones and a clear path to liquidity. Venture firms will converge on an inflection point of sorts at which a company possess enough data to support investment. Executives should identify what that inflection point is to position the company's capital raise appropriately. Valuations will vary according to the stage of the company.

- How large were the financings?

Significance: Equity investments are made with the intention of getting a firm to its next value-inflection milestone. VCs have typically "done the math" to assess how much capital will be deployed to bring the company to its next milestone. If a company's financing strategy is wildly different from other benchmarks in the sector, executives may want to align with market norms.

- Did the targets that received VC funding have any third-party validation (eg corporate sponsor, joint R&D, partnerships, etc)?

Significance: Very often, life science companies that have failed at raising capital will express their frustration with the venture market, citing their technology as being superior to what has already been funded. However, if the perceived inferior technology has been granted some type of third-party validation in the form of strategic partnerships or existing corporate sponsors, venture firms will view these firms as being significantly more "de-risked" than the supposedly superior technology.

- How many exits have there been in your sector in the past two years and at what stage of development did they occur?

Significance: Investors seek only one thing: a return on their investment. If there have been exits, then this should be clearly communicated and done early in the capital raising process. Similarly, if exits are occurring at a development stage that is beyond what your desired capital raise will power, it is likely your capital needs are too small to attract institutional investors who are wary of being "cramped down" by a necessary follow-on investment to get your firm to its exit window.

- Who are the VCs that already have an investment, made or lost money in your sector?

Significance: Investors who exited in your sector will be positively predisposed to making another investment. Conversely, those who lost money are less likely to participate in a financing round. Similarly, those who have an active company in their portfolio will more likely avoid multiple shots on goal and thus shy away from an additional investment.

- How much capital does a particular target VC firm have and at what stage is that fund in its life cycle?

Significance: If a company needs $200 million to open an exit window, it would be better served by approaching large venture firms capable of supporting the company over the long haul through multiple rounds of financing. Small firms participating in a capital intensive proposal will not be able to commit the necessary capital, which is certain to result in board dysfunction. Similarly, venture capitalists tend to deploy most of their capital in the first couple of years from inception, leaving some capital for follow-on investment. Consequently, younger funds have a higher propensity and deeper pockets to deploy capital.

- What is the core expertise of a particular target VC firm?

Significance: An investor with core expertise in your area is not only more likely to invest but will also be in a position to provide much-needed strategic and operational expertise at the board level as well as providing a network of relevant strategic players.

- Who does a particular fund syndicate with?

Significance: To manage risk, VCs typically co-invest with other VCs. Naturally, VCs develop relationships with other VCs over the years and, as such, co-invest in multiple companies. Management can exploit this fact when searching for a lead investor, thereby increasing the probability of investment.

These questions will both help to gauge the company's position in the market and assess the likelihood of a successful financing event. Most, if not all, repeatedly successful CEOs will have their teams strain to keep a constant pulse on the venture market (the most successful CEOs will also have counsel in the form of outside advisory services).

In conclusion, we suggest a few remedies that management teams might wish to adopt if a current strategy is incongruent with existing market dynamics:

1. **Adjust**: plan to adjust your strategy, sometimes significantly, but do so quickly after considering the data. Decisions might be unpopular and difficult, but running out of cash is decidedly fatal.
2. **Move On**: Do not approach the same VCs again with a newly baked strategy unless you come in with another investor they have a history of co-investing with. Better yet, wait for the new investor to make the introduction.
3. **Position**: align yourself with what the market is rewarding in terms of value propositions. Dismiss those that may be outliers (eg Theranos, Grail) and concentrate on what the market is supporting.
4. **Streamline**: communicate a clear relationship between time, capital requirement and milestones. Ensure a financing strategy toward an exist milestone.

By adopting an external view towards venture financing, a company will conserve resources while increasing the probability of success.