



## **Trends in Terms of Venture Financings In Silicon Valley (Second Quarter 2010)**

**Background** – We analyzed the terms of venture financings for 126 companies headquartered in Silicon Valley that reported raising money in the second quarter of 2010.

### **Overview of Fenwick & West Results**

- Up rounds exceeded down rounds in 2Q10 55% to 27%, with 18% of rounds flat. This was an improvement over 1Q10, when up rounds exceeded down rounds 49% to 32%, with 19% of rounds flat. This was the fourth quarter in a row in which up rounds exceeded down rounds.
- The Fenwick & West Venture Capital Barometer showed an average price increase of 30% in 2Q10, compared to 21% in 1Q10. This was also the fourth quarter in a row in which the Barometer was positive.
- The results by industry are set forth below. In general, the cleantech, software and internet/digital media industries had the best valuation-related results in 2Q10, while the life science and hardware industries trailed.

### **Overview of Other Industry Data**

Third party analysis of the venture industry in the second quarter of 2010 reported a significant increase in venture investment, mild improvement in venture funded company liquidity, and continued difficulty in capital-raising by venture funds. Detailed results are as follows:

- DowJones VentureSource (“VentureSource”) reported that the amount invested by venture capitalists in the U.S. in the second quarter of 2010 was approximately \$7.7 billion in 744 deals, a significant increase from the \$4.7 billion invested in 602 deals in 1Q10. The PwC/NVCA MoneyTree™ report based on data from Thomson Reuters (the “MoneyTree™ Report”) also reported a significant increase in 2Q10 venture capital investment, with \$6.5 billion invested in 906 deals, compared to \$4.9 billion invested in 740 deals in 1Q10. The increase in investment was led by the life science and cleantech industries, and the largest venture deal in the quarter was a \$350 million round raised by Better Place.
- VentureSource reported 79 acquisitions of venture-backed companies in the U.S. in 2Q10, for a total of \$4.3 billion, a reduction from the \$6.0 billion paid in 103 acquisitions currently being reported for 1Q10, but a slight increase from the 77 acquisitions for a total of \$4.0 billion initially reported for 1Q10 at the end of 1Q10. Thomson Reuters and the National Venture Capital Association reported 92 acquisitions of venture-backed companies in the second quarter of 2010, compared to 119 currently being reported for 1Q10, and 111 initially reported at the end of 1Q10. As VentureSource and Thomson Reuters/NVCA initially publish data approximately 3-4 weeks after the end of each quarter, and then continue to update their results for the quarter as new

information becomes available, for quarter to quarter comparison purposes it may be best to use the initially reported amounts for each quarter until final amounts are available for the later quarter. The largest acquisition in 2Q10 was Google's acquisition of AdMob for \$750 million.

- There were 17 venture-backed IPOs in the second quarter of 2010, compared to 9 in 1Q10, marking the third consecutive quarter for increased offerings and the best quarterly total since the fourth quarter of 2007, according to Thomson Reuters and the National Venture Capital Association. Nine of the IPOs were in the information technology industry. The IPOs raised \$1.3 billion and 45 venture-backed companies were in registration for an initial public offering with the SEC as of June 30, 2010. VentureSource reported 15 venture-backed IPOs in 2Q10 raising a total of \$900 million, compared to eight IPOs raising \$710 million in 1Q10. The largest IPO in 2Q10 was Tesla Motors raising \$226 million.
- Fundraising by U.S. venture capital firms declined in the second quarter, with 38 firms raising \$1.9 billion in the quarter, compared to 38 firms raising \$3.7 billion in the first quarter of 2010, according to Thomson Reuters and the National Venture Capital Association. The largest fundraising in 2Q10 was \$325 million by Venrock Associates VI.
- The 2010 Global Venture Capital Survey by Deloitte and the National Venture Capital Association reported that over 90% of U.S. venture capitalists surveyed expect the number of venture firms in the U.S. to decrease between now and 2015. The primary reasons cited were difficulty in achieving successful exits, unfavorable tax policy and an unstable regulatory environment. However, U.S. venture capitalists were of mixed opinion regarding valuations over the next five years with 32% expecting increases, 34% expecting decreases and 34% expecting flat valuations. Overseas, a majority of venture capitalists in China, India and Brazil expected to see an increase in venture firms in their countries over the next five years.
- The Silicon Valley Venture Capital Index reported by Professor Mark Cannice at the University of San Francisco reported the confidence level of Silicon Valley venture capitalists at 3.28 on a 5 point scale, which is a significant drop from the previous quarter's reading of 3.65, and ended a five-quarter upward trend in VC confidence since its low point in 4Q08.
- The Wall Street Journal reported on July 19, 2010, based on research from Preqin, a research firm, that U.S. venture capital funds raised each year from 1999 to 2007 have posted median annualized returns averaging from a 0.3% gain to a 7.7% loss.
- 40% of all U.S. venture capital investment in 2Q10 was in Northern California, and 50% of all investment was in California as a whole, according to VentureSource.
- Nasdaq was down 12.8% in Q2 but up 8.7% in Q3 through August 6, 2010.

## Detailed Fenwick & West Results

**Financing Round** – The financings broke down according to the following rounds:

Series	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
A	18%	24%	23%	17%	8%	13%	16%	16%
B	22%	21%	22%	31%	27%	28%	26%	26%
C	28%	30%	21%	19%	35%	17%	29%	28%
D	20%	11%	17%	16%	13%	20%	14%	17%
E and higher	12%	14%	17%	17%	17%	22%	15%	13%

**Price Change** – The direction of price changes for companies receiving financing this quarter, compared to their previous round, were as follows:

Price Change	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
Down	27%	32%	30%	36%	46%	46%	33%	12%
Flat	18%	19%	23%	23%	22%	29%	13%	15%
Up	55%	49%	47%	41%	32%	25%	54%	73%

The percentage of down rounds by series were as follows:

Series	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
B	14%	23%	24%	19%	16%	38%	21%	7%
C	29%	45%	25%	45%	51%	50%	43%	14%
D	36%	18%	47%	56%	67%	39%	22%	12%
E and higher	33%	27%	26%	39%	67%	60%	45%	15%

**The Fenwick & West Venture Capital Barometer™ (Magnitude of Price Change)** –Set forth below is (i) for up rounds, the average per share percentage increase over the previous round, (ii) for down rounds, the average per share percentage decrease over the previous round, and (iii) the overall average per share percentage change from the previous round for all rounds taken together. Such information is broken down by series for 2Q10 and is provided on an aggregate basis for comparison purposes for the prior four quarters. In calculating the “net result” for all rounds, “flat rounds” are included. For purposes of these calculations, all financings are considered equal, and accordingly the results are not weighted for the amount raised in a financing.

Percent Change	Series B	Series C	Series D	Series E and higher	Combined total for all Series for Q2'10	Combined total for all Series for Q1'10	Combined total for all Series for Q4'09	Combined total for all Series for Q3'09	Combined total for all Series for Q2'09
Up rounds	+118%	+78%	+51%	+87%	+86%	+78%	+73%	+77%	+61%
Down rounds	-64%	-64%	-69%	-60%	-65%	-54%	-50%	-57%	-54%
Net result	+67%	+29%	Flat	+15%	+30%	+21%	+19%	+11%	-6%

**Results by Industry for Price Changes and Fenwick & West Venture Capital Barometer™** – The table below sets forth the direction of price changes and Barometer results for companies receiving financing in 2Q10, compared to their previous round, by industry group. Companies receiving Series A financings are excluded as they have no previous rounds to compare.

Industry	Number of Financings	Up Rounds	Down Rounds	Flat Rounds	Barometer
Software	34	73%	21%	6%	+51%
Hardware	14	29%	36%	35%	-7%
Lifescience	23	48%	22%	30%	+4%
Internet/Digital Media	23	52%	35%	13%	+43%
Cleantech	7	57%	29%	14%	+59%
Other	2	50%	50%	0%	-18%
<b>Total - All Industries</b>	103	55%	27%	18%	+30%

Please note that some industries have small sample sizes that reduce the statistical validity of the results.

**Liquidation Preference** – Senior liquidation preferences were used in the following percentages of financings:

Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
40%	38%	41%	49%	41%	45%	41%	45%

The percentage of senior liquidation preference by series was as follows:

Series	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
B	32%	23%	24%	38%	17%	35%	30%	35%
C	34%	42%	50%	40%	52%	38%	35%	48%
D	48%	36%	58%	63%	50%	56%	61%	59%
E and higher	53%	53%	37%	67%	53%	55%	50%	38%

**Multiple Liquidation Preferences** - The percentage of senior liquidation preferences that were multiple preferences were as follows:

Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
17%	23%	19%	21%	24%	28%	23%	16%

Of the senior liquidation preferences that included a multiple preference, the ranges of the multiples broke down as follows:

Range of multiples	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
>1x- 2x	71%	86%	57%	89%	75%	80%	70%	50%
>2x – 3x	29%	14%	43%	11%	25%	10%	20%	50%
> 3x	0%	0%	0%	0%	0%	10%	10%	0%

**Participation in Liquidation** – The percentages of financings that provided for participation were as follows:

Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
35%	48%	51%	53%	49%	51%	57%	62%

Of the financings that had participation, the percentages that were not capped were as follows:

Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
61%	54%	54%	60%	67%	60%	51%	51%

The decrease in use of participating liquidation preference was due to a significant decrease in the use of that provision in Series A rounds this quarter.

**Cumulative Dividends** – Cumulative dividends were provided for in the following percentages of financings:

Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
7%	7%	4%	7%	2%	10%	4%	4%

**Antidilution Provisions** – The uses of antidilution provisions in the financings were as follows:

Type of Provision	Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
Ratchet	4%	5%	6%	3%	3%	3%	2%	7%
Weighted Average	94%	94%	94%	96%	97%	97%	98%	93%
None	2%	1%	0%	1%	0%	0%	0%	0%

**Pay-to-Play Provisions** – The use of pay-to-play provisions in the financings was as follows:

Percentages of financings having pay-to-play provisions.

Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
16%	7%	10%	15%	15%	14%	15%	12%

Note that anecdotal evidence indicates that companies are increasingly using contractual “pull up” provisions instead of charter based “pay to play” provisions. These two types of provisions have similar economic effect but are implemented differently. The above information includes some, but likely not all, pull up provisions, and accordingly may understate the use of these provisions.

The pay-to-play provisions provided for conversion of non-participating investors’ preferred stock into common stock or shadow preferred stock, in the percentages set forth below:

- Common Stock.

Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
100%	86%	80%	93%	100%	73%	85%	60%

- Shadow Preferred Stock.

Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
0%	14%	20%	7%	0%	27%	15%	40%

**Redemption** – The percentages of financings providing for mandatory redemption or redemption at the option of the venture capitalist were as follows:

Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
23%	24%	21%	19%	20%	24%	20%	23%

**Corporate Reorganizations** – The percentages of post-Series A financings involving a corporate reorganization were as follows:

Q2'10	Q1'10	Q4'09	Q3'09	Q2'09	Q1'09	Q4'08	Q3'08
8%	14%	5%	8%	10%	10%	13%	4%

For additional information about this report please contact Barry Kramer at 650-335-7278; [bkramer@fenwick.com](mailto:bkramer@fenwick.com) or Michael Patrick at 650-335-7273; [mpatrick@fenwick.com](mailto:mpatrick@fenwick.com) at Fenwick & West. The contents of this report are not intended, and should not be considered, as legal advice or opinion.

**To be placed on an email list for future editions of this survey please go to our [VC Survey sign up page](#).**