



Trends in Terms of Venture Financings In the San Francisco Bay Area (Third Quarter 2007)

- **Background** – We analyzed the terms of venture financings for 104 companies headquartered in the San Francisco Bay Area that reported raising money in the third quarter of 2007.
- **Overview**

The results of the 3Q07 survey showed a continuation of the strong positive trend in venture valuations. The highlights of the quarter are as follows:

- Up rounds exceeded down rounds for the 15th quarter in a row (79% up vs. 14% down, with 7% flat).
- The Fenwick & West Venture Capital Barometer™ showed a 79% average price increase for companies receiving venture capital in 3Q07, compared to such companies' prior financing round. This was the largest increase since our survey began. This increase was driven in part by 9 financings in which the purchase price of the stock sold in the financing was at least 3 times higher than prior round. Of these financings, 3 were in Web 2.0 and related fields and 3 were in Cleantech.

Other U.S. venture industry related results for the third quarter included the following:

- The amount invested by venture capitalists in the U.S. in 3Q07 was approximately \$8.1 billion in 635 transactions, compared to \$7.5 billion raised in 727 transactions in 2Q07. The amount invested in 3Q07 was the highest amount of venture investment in a quarter since 1Q01.¹
- Venture investment in health care continued to be strong accounting for \$2.5 billion of total investment in 3Q07. Health care companies have raised \$7.9 billion in 2007 through the third quarter, of which \$2.9 billion was in medical device companies. The amount raised by medical device companies in YTD 2007 is more than they have raised in any prior full year. Information technology investments continued to be the largest investment area overall, raising \$3.8 billion, with information services companies (which includes Web. 2.0 companies) again attracting close to \$1 billion in investments during 3Q07. Cleantech was also strong, raising \$848 million in 3Q07.¹

- Acquisitions of venture backed companies in 3Q07 increased notably, with 90 transactions totaling \$10.5 billion, compared to 89 transactions totaling \$8.1 billion in 2Q07. This was the highest quarterly acquisition activity in dollar terms since 2000. The number of acquisitions has actually declined some, resulting in the median acquisition price increasing significantly in YTD 2007, from \$51 million in 2006 to \$89 million in 2007 year to date. IT accounted for \$7.4 billion of acquisitions and health care accounted for \$2.3 billion of the total. The time from initial financing to M&A increased to seven years, the highest level on record.¹
- IPOs of venture backed companies decreased to 11 companies raising \$0.7 billion in 3Q07, compared to 24 IPOs raising \$2.8 billion in 2Q07.¹
- Nasdaq was up 2.6% in 3Q07, but is down 2.3% in 4Q07 to date. Increasing concern regarding credit and dollar issues, international political stability, and the upcoming U.S. elections, may be creating uncertainty as to the future.

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

Series	Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
A	13%	14%	18%	22%	23%	14%	11%	22%
B	38%	34%	38%	31%	31%	34%	40%	35%
C	28%	25%	20%	23%	24%	28%	17%	17%
D	12%	18%	12%	11%	17%	16%	15%	11%
E and higher	9%	9%	12%	13%	5%	8%	17%	15%

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

Price Change	Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
Down	14%	11%	9%	22%	24%	25%	15%	19%
Flat	7%	8%	12%	11%	9%	6%	11%	12%
Up	79%	81%	79%	67%	67%	69%	74%	69%

The percentage of down rounds by series were as follows:

Series	Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
B	13%	5%	7%	6%	13%	16%	12%	10%
C	14%	10%	4%	15%	24%	32%	12%	5%
D	8%	17%	0%	42%	38%	14%	27%	46%
E and higher	33%	27%	36%	53%	33%	57%	12%	35%

- **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 Q3'07 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.

Q3'07

Percent Change	Series B	Series C	Series D	Series E and higher	Combine d total for all Series for Q3'07	Combine d total for all Series for Q2'07	Combine d total for all Series for Q1'07	Combine d total for all Series for Q4'06	Combine d total for all Series for Q3'06
Up rounds	+155%	+83%	+39%	+69%	+108%	+99%	+100%	+100%	+86%
Down rounds	-40%	-65%	-18%	-40%	-46%	-46%	-47%	-49%	-35%
Net result	+122 %	+63%	+29%	+17%	+79%	+74%	+75%	+69%	+49%

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

Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
42%	51%	36%	40%	42%	50%	40%	41%

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

Series	Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
B	23%	47%	30%	23%	30%	35%	29%	22%
C	48%	39%	25%	38%	41%	76%	47%	40%
D	69%	65%	50%	58%	57%	36%	60%	69%
E and higher	67%	74%	64%	67%	67%	57%	41%	65%

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

Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
21%	15%	14%	14%	26%	16%	14%	24%

Of the senior liquidation preferences, the ranges of the multiples broke down as follows:

Range of multiples	Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
>1x- 2x	100%	75%	100%	40%	90%	83%	80%	67%
>2x – 3x	0%	25%	0%	60%	10%	0%	20%	33%
> 3x	0%	0%	0%	0%	0%	17%	0%	0%

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

Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
54%	48%	59%	73%	64%	71%	65%	64%

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

Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
39%	54%	52%	64%	58%	64%	55%	50%

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

financings:

Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
4%	6%	8%	4%	7%	8%	3%	4%

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

Type of Provision	Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
Ratchet	6%	5%	5%	4%	4%	2%	4%	9%
Weighted Average	94%	93%	94%	95%	95%	97%	92%	85%
None	0%	2%	0%	1%	1%	1%	4%	6%

- **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.

Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
13%	10%	8%	10%	10%	16%	11%	16%

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.

Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
57%	77%	89%	73%	50%	86%	73%	89%

- Shadow Preferred Stock.

Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
43%	23%	11%	27%	50%	14%	27%	11%

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

Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
26%	22%	26%	22%	29%	33%	27%	31%

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

Q3'07	Q2'07	Q1'07	Q4'06	Q3'06	Q2'06	Q1'06	Q4'05
9%	3%	9%	6%	5%	12%	9%	11%

For additional information about this report please contact Barry Kramer at 650-335-7278; bkramer@fenwick.com or Michael Patrick at 650-335-7273; mpatrick@fenwick.com at Fenwick & West. To be placed on an email list for future editions of this survey please go to our [VC Survey sign up page](#). The contents of this report are not intended, and should not be considered, as legal advice or opinion.

¹ Information in this paragraph obtained from Dow Jones VentureSource.

