3Q13

Trends in Terms of Venture Financings in Silicon Valley

Third Quarter 2013

Fenwick
FENWICK & WEST LLP

Silicon Valley Venture Capital Survey
Third Quarter 2013

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Background

We analyzed the terms of venture financings for 128 companies headquartered in Silicon Valley that reported raising money in the third quarter of 2013.

Overview of Fenwick & West Results

Valuation results in 3Q13 showed a noticeable increase over 2Q13, including the greatest difference between up and down rounds in over six years. The software industry was especially strong, not only valuation-wise, but also in the number of deals.

Here are the more detailed results:

- Up rounds exceeded down rounds 73% to 8%, with 19% of rounds flat. This was a significant increase from 2Q13 when up rounds exceeded down rounds 64% to 22% with 14% flat, and the best quarter (measured by amount by which up rounds exceeded down rounds) since 3Q07.
- The Fenwick & West Venture Capital Barometer™ showed an average price increase of 65% in 3Q13, an increase from the 62% reported in 2Q13.
- The median price increase of financings in 3Q13 was 43%, a noticeable increase from the 19% and 14% reported in 2Q13 and 1Q13, respectively.
- The results by industry are set forth below. In general internet/digital media slightly edged out software for best valuation performance, although there were significantly more software deals than internet/digital media, as software deals were 53% of all deals, the highest amount since we began tracking results by industry in 1Q10. Life Science fell to 10.2% of all deals, the lowest percentage since 1Q10.
- The percentage of financings with participating liquidation preference was 27%, the lowest amount since we began our survey in 2002 and an indication of an entrepreneur friendly environment.

Overview of Other Industry Data

Overall the venture environment improved in 3Q13, but due to a slow start 2013 lags 2012 in some categories.

- Venture investing in 3Q13 increased, bringing the first three quarters of 2013 approximately even with 2012, although trailing 2011.
- IPOs were again strong in 3Q13. Although 2013 is expected to be the best year for venture backed IPOs since 2007, much of the increase through the first three quarters has been focused in the life science sector.
- M&A improved noticeably in 3Q13, but 2013 is on track to have the lowest number of acquisitions of venture backed companies since 2009.
- Venture fundraising improved over a weak 2Q13, but 2013 was on track to be the lowest fundraising year since 2010.

- Corporate venture capital participation continued to increase.
- Angel financing results were mixed. And with new more liberal regulations regarding public solicitations and crowd funding, the angel financing world is likely in for some changes.
- Venture capitalist sentiment hit the highest level since the 2008 recession.

The more detailed results follow:

- **Venture Capital Investment**

  Dow Jones VentureSource ("VentureSource") reported a 12.5% increase in venture investment and a 1% increase in the number of venture financings from 2Q13 to 3Q13. Specifically, $8.1 billion was invested in 806 deals in 3Q13 compared to $7.2 billion invested in 801 deals in 2Q13 (as reported in July 2013).[1] This was the largest amount invested in a quarter since 2Q12. Google Ventures was the most prolific investor funding 23 deals.

  Similarly, the PwC/NVCA MoneyTree™ Report based on data from Thomson Reuters (the "MoneyTree Report") reported a 16% increase in venture investment and a 10% increase in the number of financings from 2Q13 to 3Q13. They reported $7.8 billion raised in 1005 deals in 3Q13 compared to $6.7 billion raised in 913 deals in 2Q13 (as reported in July 2013).[1] The software industry was especially active receiving $3.6 billion, the largest amount in a quarter in 12 years.

  VentureSource, MoneyTree Report and Pitchbook all noted a trend from consumer/web to business/software investing.

- **IPO Activity**

  IPO activity continued strong in 3Q13, with 25 IPOs raising $2.2 billion, compared to 18 IPOs raising $1.7 billion in 2Q13, according to VentureSource.

  Similarly, Thomson Reuters and the NVCA ("Thomson/NVCA") reported 26 IPOs raising $2.7 billion in 3Q13, compared to 23 IPOs raising $2.4 billion in 2Q13. Sixteen of the 26 IPOs were in the life sciences industry.

  VentureWire has reported that 2013 will have the largest number of venture backed IPOs since 2007 (Russ Garland, 10/7/13).

  And despite the relatively healthy after market performance of IPOs in the first three quarters of 2013, the Venture Capital Journal notes that venture capitalists appear to be holding on to their public company shares longer than they have historically.

- **Merger and Acquisition Activity**

  VentureSource reported a 21% increase in the amount paid in the acquisition of venture backed companies, and a 32% increase in the number of acquisitions, in 3Q13 compared to 2Q13. Specifically, there were 111 deals for $9.7 billion in 3Q13 compared to 84 deals for $8.0 billion in 2Q13 (as reported in July 2013).[1]

  This is consistent with Thomson/NVCA which reported a 27% increase in the number of acquisitions. Although 3Q13 was an improved quarter, the number of venture backed acquisitions in 2013 is on track to be the lowest since 2009.

Yahoo was the largest acquirer of venture backed companies in 3Q13 with four acquisitions, and Apple was second with three (VentureWire, Russ Garland, 10/7/13).

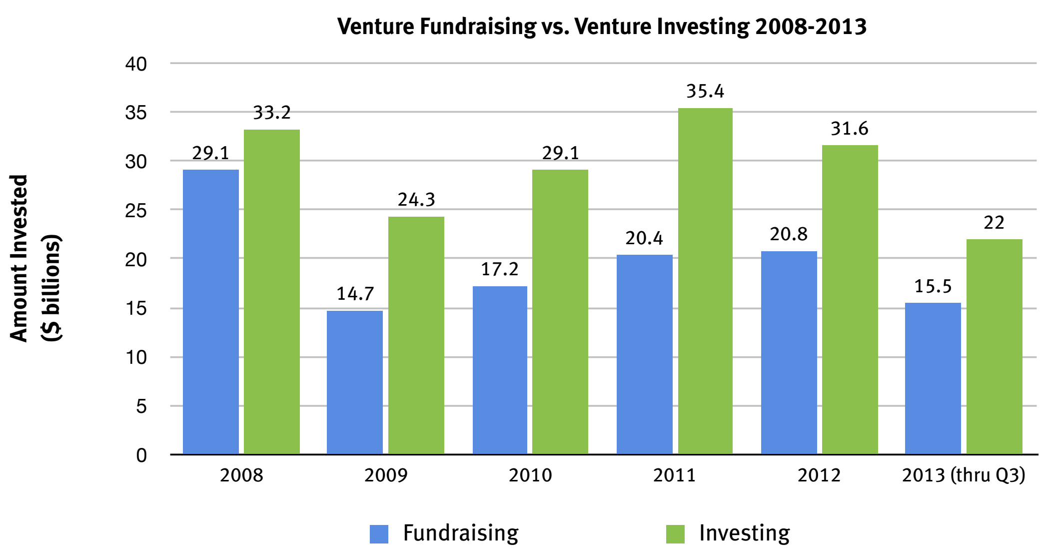
Acquisitions have provided a larger percentage return to investors than IPOs, when compared to the prior venture financing round, in 2011-13, according to Pitchbook.

- **Venture Capital Fundraising**

Thomson Reuters reported a 41% increase in dollars and a 27% increase in the number of funds raising money in 3Q13 compared to a weak 2Q13. Specifically, 56 funds raised $4.1 billion in 3Q13 compared to 44 funds raising $2.9 billion in 2Q13 (as reported in July 2013).[1] However, the first three quarters of 2013 were down 29% (in dollars) from the first three quarters of 2012, and 2013 was on track to be the lowest fundraising year since 2010.

Similarly, VentureSource reported fundraising down 11% in the first three quarters of 2013.

VentureSource also reported that in the 2008-3Q13 time period, the amount invested in venture backed US based companies outpaced US venture capital fundraising, $175 billion to $118 billion. Although some of this difference can be attributed to the years prior to 2008 when fundraising slightly outpaced investing, we believe that investments by late stage non-VC investors (e.g., private equity, cross-over and hedge funds), corporate venture capital and non-US based venture capital have increased during this period to mostly account for the difference.



Source: Dow Jones LP Source

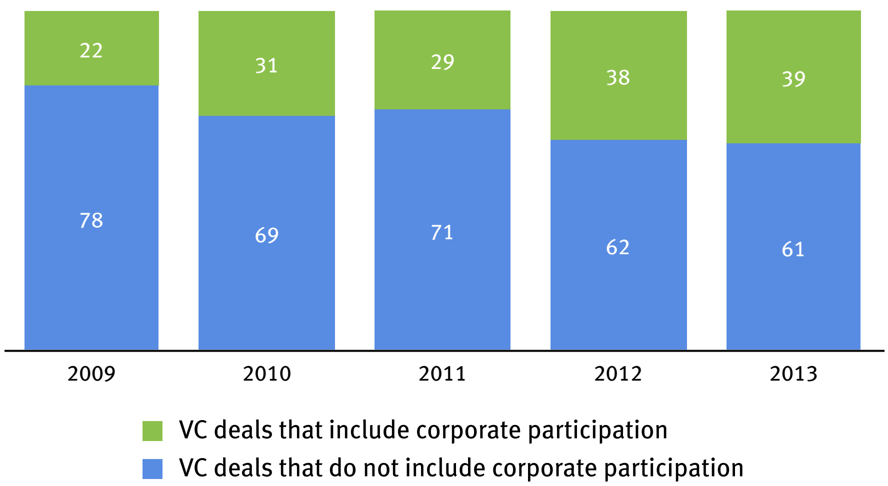
A survey by Probitas Partners reported in the Venture Capital Journal found that 39% of institutional limited partners did not invest in venture capital, twice the amount that was reported in 2007.

- **Corporate Venture Capital ("CVC")**

  Corporate venture investing appears to be continuing to increase, likely due in part to the substantial amount of cash held on corporate balance sheets. Techcrunch reports that in October 2013 CVCs participated in 14% of VC deals, the highest month in their Crunchbase dataset, with Google and Intel being the leading CVCs since 2011. And while data showed that CVCs still generally prefer later rounds, there appears to be a growing appetite for early stage investment also.

  Similarly, CB Insights reported that an analysis of the 100 largest VC backed tech deals of the past five years shows that CVC participation has increased from 22% in 2009 to 39% in 2012.

Corporate Participation in Top 100 VC-Backed Tech Deals



Source: CB Insights

- **Angel/Seed Financing**

  Data on angel financings was mixed, with the Center for Venture Research reporting that total angel investment in the first half of 2013 was 5.2% higher than the first half of 2012, but Techcrunch reporting that US angel investing in 2013 is likely to be lower than in 2012 .

  Techcrunch also reported that angel backed companies are taking longer to close their first venture rounds, with the average angel backed company that raises Series A funding taking 434 days to raise a Series A round in 2012, compared to 526 days in 2013. But this may not be because of increased difficulty in raising Series A funding, as larger angel rounds allow companies to wait longer, and Techcrunch reports that the number of Series A deals increased more than the number of angel rounds in 2013, compared to 2012.

  With changes in the law allowing more liberal public solicitations and crowd funding of start ups, the angel financing world may undergo some significant changes in the future.

- **Venture Capital Return**

  Cambridge Associates reported that the value of its venture capital index increased by 4.3% in 2Q13 (3Q13 results have not been publicly released), which was about even with the Nasdaq increase of 4.15%. For longer time frames, the Nasdaq surpassed the venture index over the last 1, 3 and 5 years, but for periods beyond 10 years the venture index substantially outpaced Nasdaq.

- **Venture Capital Sentiment**

  The Silicon Valley Venture Capitalists Confidence Index® by Professor Mark Cannice at the University of San Francisco reported that the confidence level of Silicon Valley venture capitalists rose to 3.92 on a 5 point scale, the highest level since the global financial crisis in 2007/08. Reasons given included reasonable valuations, strong cloud, big data and mobility opportunities, and improvement in the liquidity outlook. Concerns cited included government dysfunction, difficulty in raising funds, and problems specific to the life science industry.

- **Venture Trends**

  The top three universities producing US venture capital backed entrepreneurs in the 2010-2013 period were Stanford, UC Berkeley and Penn according to Pitchbook. The Indian Institutes of Technology made the list at #10.

  Pitchbook also reported that the percentage of companies backed by venture capital with at least one woman founder increased from 4% in 2004 to 13% currently. Venture backed women entrepreneurs were highest in the consumer and retail industries, with software lagging.

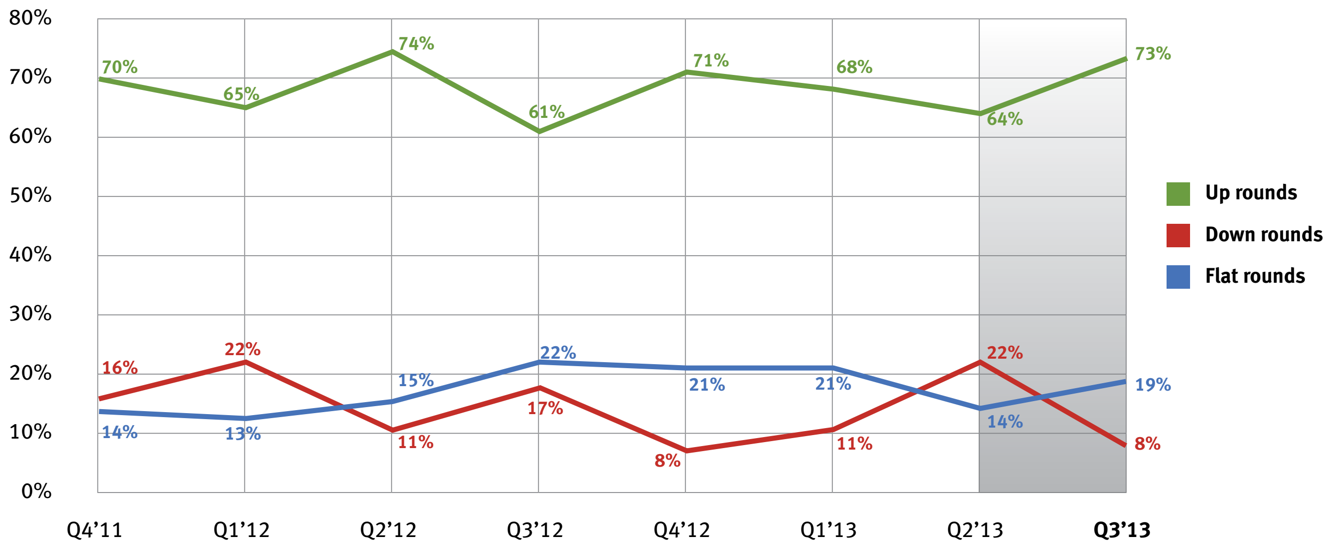
  A recent Wall Street Journal article noted that the top business schools are sending an increasing percentage of their graduates to the tech sector as opposed to financial services. At Stanford in 2013 tech employment overtook financial services for the first time – 32% vs. 26%, and at Harvard, while financial services still led, the lead has decreased from 35% vs. 12% in 2012, to 27% vs. 18% in 2013. (Melissa Korn, 11/5/13)

- **Nasdaq**

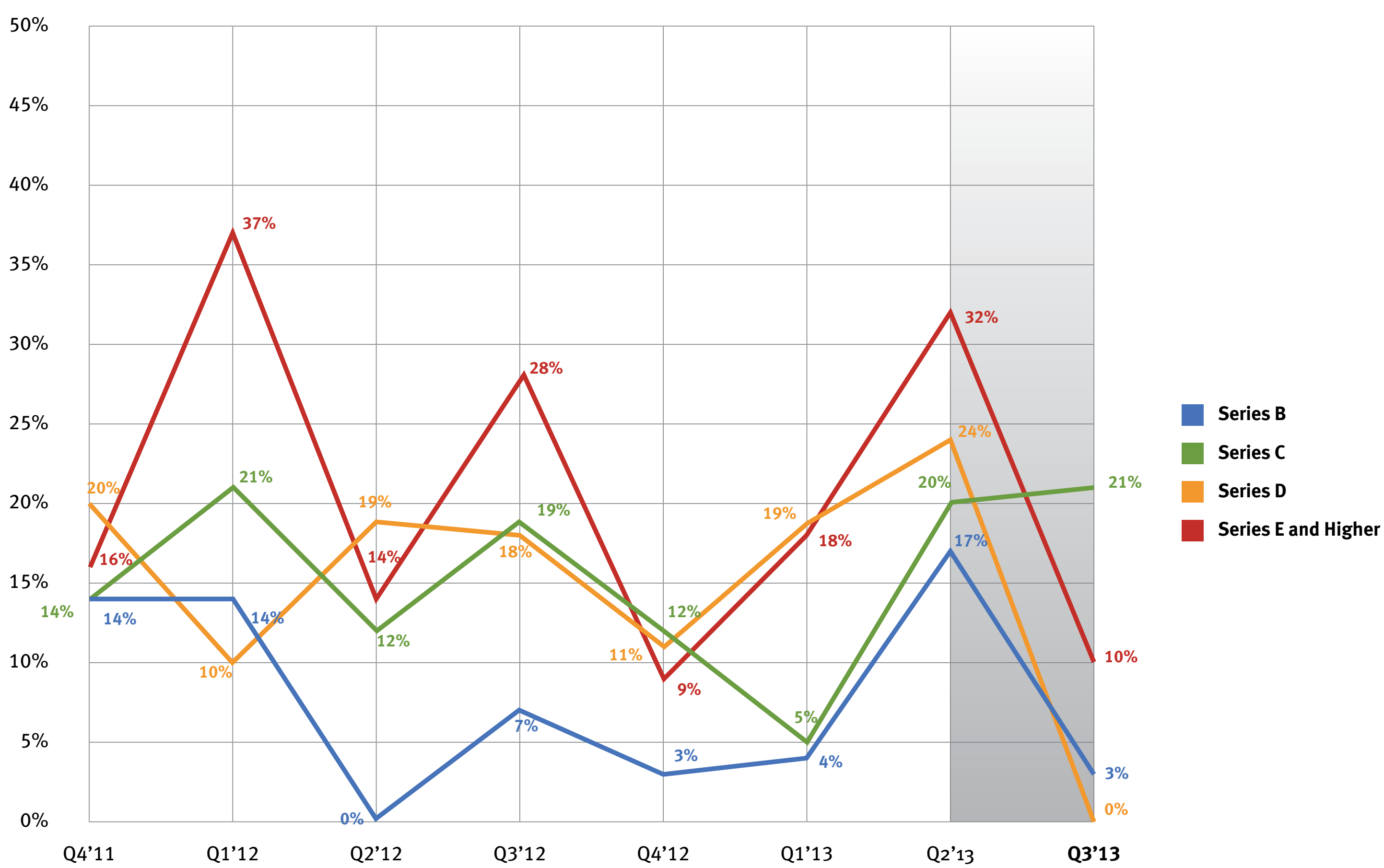
  Nasdaq increased 9.9% in 3Q13, and has increased an additional 3.8% in 4Q13 through November 10, 2013.

Fenwick & West Data on Valuation

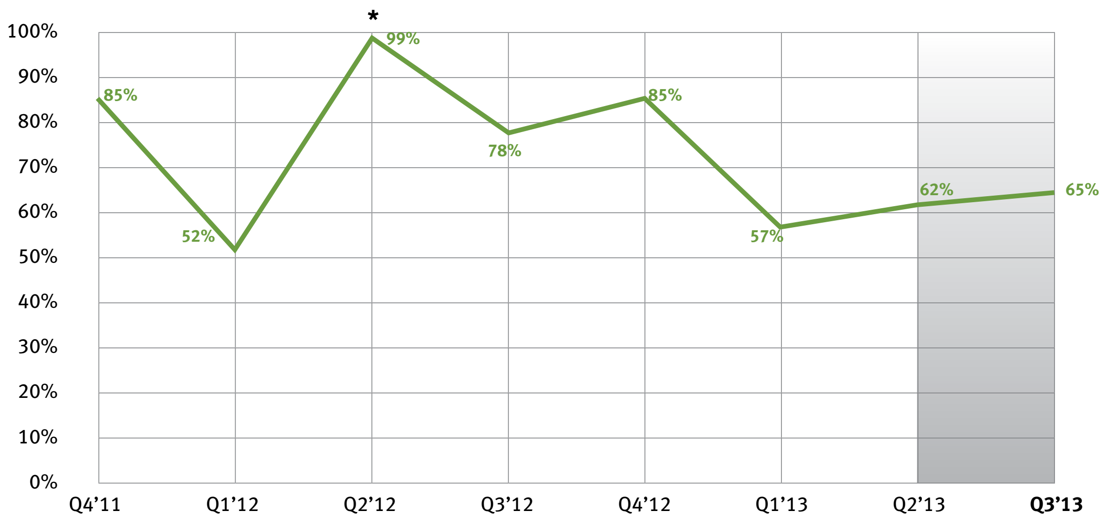
PRICE CHANGE—The direction of price changes for companies receiving financing in a quarter, compared to their prior round of financing.



The percentage of down rounds by series were as follows:

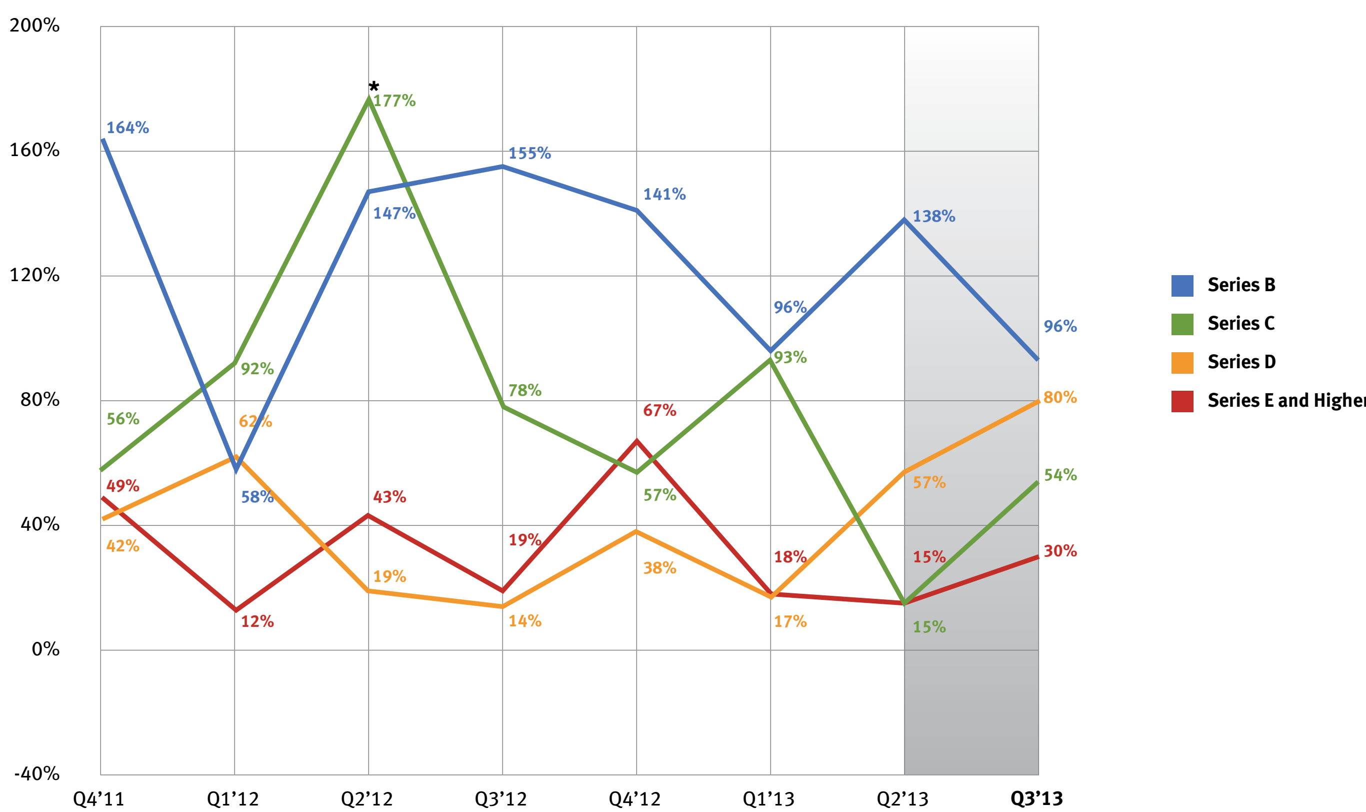


THE FENWICK & WEST VENTURE CAPITAL BAROMETER™ (MAGNITUDE OF PRICE CHANGE) — Set forth below is the average percentage change between the price per share at which companies raised funds in a quarter, compared to the price per share at which such companies raised funds in their prior round of financing. In calculating the average, all rounds (up, down and flat) are included, and results are not weighted for the amount raised in a financing.



* One software company had a 1460% up round and one internet/digital media company had a 1190% up round in 2Q12. If these were excluded the Barometer result for 2Q12 would have been 70%.

The Barometer results by series are as follows:



* Please note that the two above mentioned software and internet/digital media companies with greater than 10x up rounds in 2Q12 were both Series C rounds. If these were excluded the Barometer result for Series C rounds in 2Q12 would have been 72%.

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 3Q13, compared to their previous round, by industry group. Companies receiving Series A financings are excluded as they have no previous rounds to compare.

Industry	Up Rounds	Down Rounds	Flat Rounds	Barometer	Number of Financings
Software	81%	5%	14%	71%	57
Hardware	36%	27%	37%	28%	10
Life Science	40%	20%	40%	34%	5
Internet/Digital Media	89%	5%	6%	91%	18
Cleantech	33%	0%	67%	15%	3
Other	75%	25%	0%	24%	4
Total all Industries	**74%**	**9%**	**17%**	**64%**	**97**

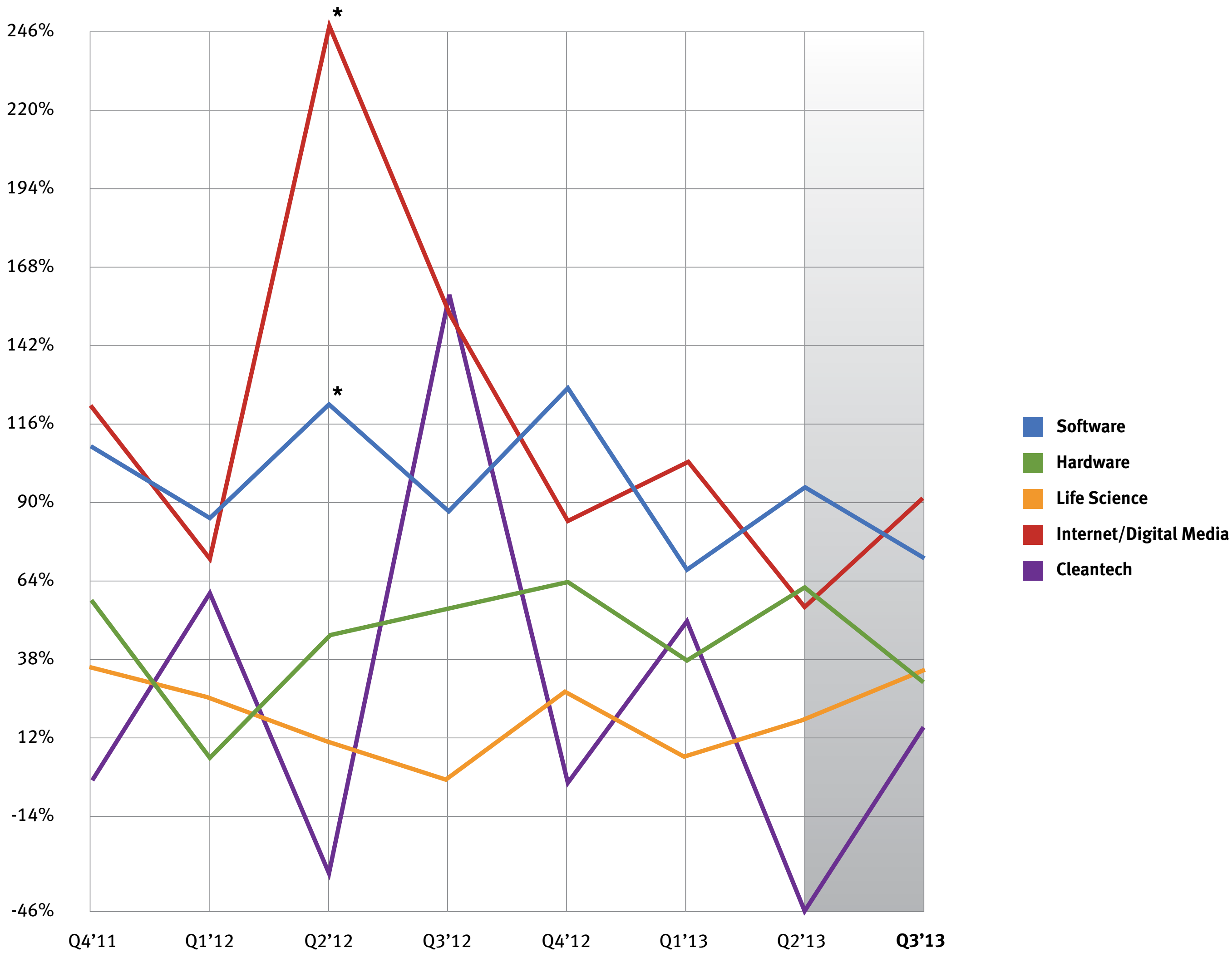
DOWN ROUND RESULTS BY INDUSTRY — The table below sets forth the percentage of "down rounds," by industry groups, for each of the past eight quarters.

Down Rounds	Q4'11	Q1'12	Q2'12	Q3'12	Q4'12	Q1'13	Q2'13	Q3'13
Software	11%	14%	8%	11%	5%	10%	20%	5%
Hardware	0%	42%	15%	30%	8%	0%	9%	20%
Life Science	33%	24%	6%	21%	10%	33%	30%	20%
Internet/Digital Media	12%	20%	0%	14%	12%	6%	16%	5%
Cleantech	43%	0%	75%	0%	17%	0%	100%	0%
Other	0%	0%	50%	0%	0%	0%	50%	25%
Total all Industries	**16%**	**22%**	**11%**	**17%**	**8%**	**11%**	**22%**	**8%**

BAROMETER RESULTS BY INDUSTRY — The table below sets forth Barometer results by industry group for each of the last eight quarters.

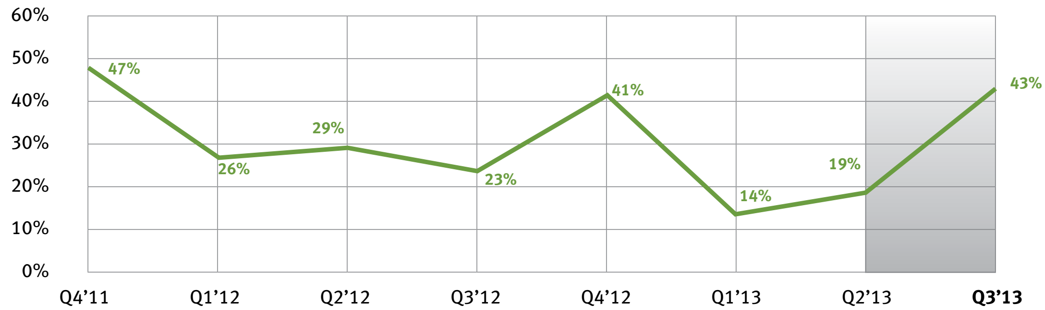
Barometer	Q4'11	Q1'12	Q2'12	Q3'12	Q4'12	Q1'13	Q2'13	Q3'13
Software	105%	85%	123%*	87%	128%	67%	95%	71%
Hardware	58%	5%	46%	55%	64%	38%	62%	30%
Life Science	36%	26%	11%	-2%	30%	6%	20%	34%
Internet/Digital Media	122%	72%	248%*	153%	85%	103%	56%	91%
Cleantech	-3%	61%	-33%	158%	-2%	51%	-46%	15%
Total all Industries	**85%**	**52%**	**99%**	**78%**	**85%**	**57%**	**62%**	**65%**

A graphical representation of the above is below.



* These include the two previously mentioned companies with greater than 10x up rounds in 2Q12. Excluding those two companies, the Barometer result for the software industry would have been 86% and the Barometer result for the internet/digital media industry would have been 176%.

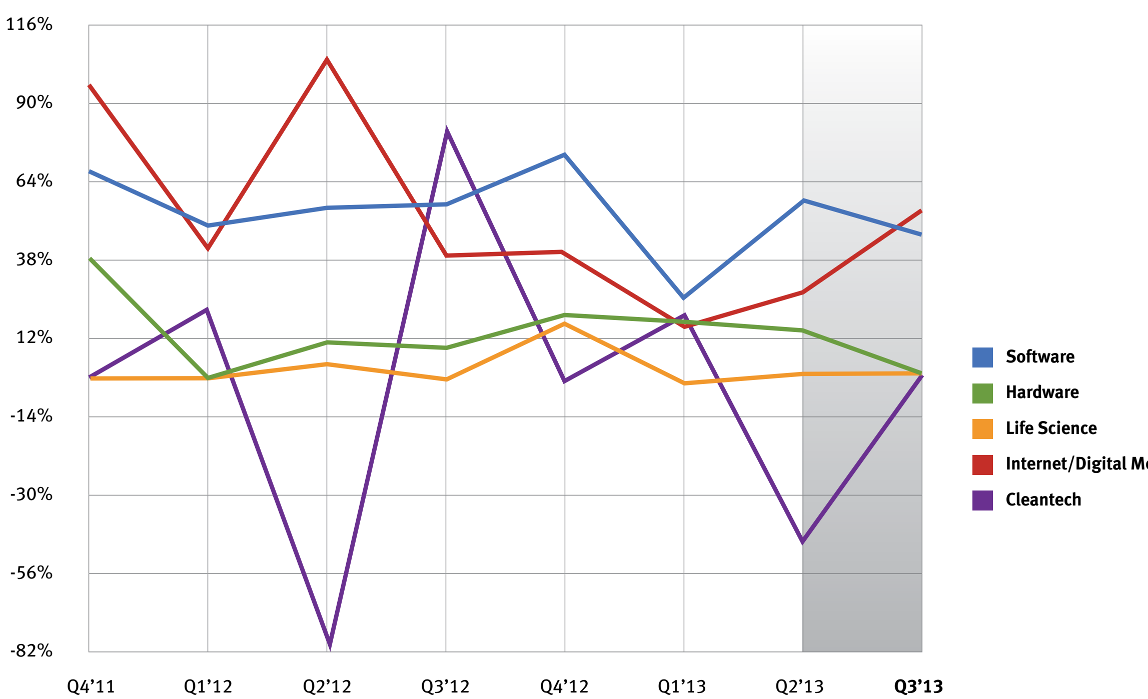
MEDIAN PERCENTAGE PRICE CHANGE—Set forth below is the median percentage change between the price per share at which companies raised funds in a quarter, compared to the price per share at which such companies raised funds in their prior round of financing. In calculating the median, all rounds (up, down and flat) are included, and results are not weighted for the amount raised in the financing. Please note that this is different than the Barometer, which is based on average percentage price change.



MEDIAN PERCENTAGE PRICE CHANGE RESULTS BY INDUSTRY —The table below sets forth the median percentage price change results by industry group for each of the last eight quarters. Please note that this is different than the Barometer, which is based on average percentage price change.

Barometer	Q4'11	Q1'12	Q2'12	Q3'12	Q4'12	Q1'13	Q2'13	Q3'13
Software	67%	50%	56%	57%	74%	25%	58%	46%
Hardware	38%	0%	11%	10%	20%	17%	15%	0%
Life Science	0%	0%	5%	0%	17%	0%	0%	0%
Internet/Digital Media	96%	41%	105%	39%	41%	16%	28%	54%
Cleantech	0%	21%	-82%	79%	0%	18%	-46%	0%
Total all Industries	**47%**	**26%**	**29%**	**23%**	**41%**	**14%**	**19%**	**43%**

A graphical representation of the above is below.

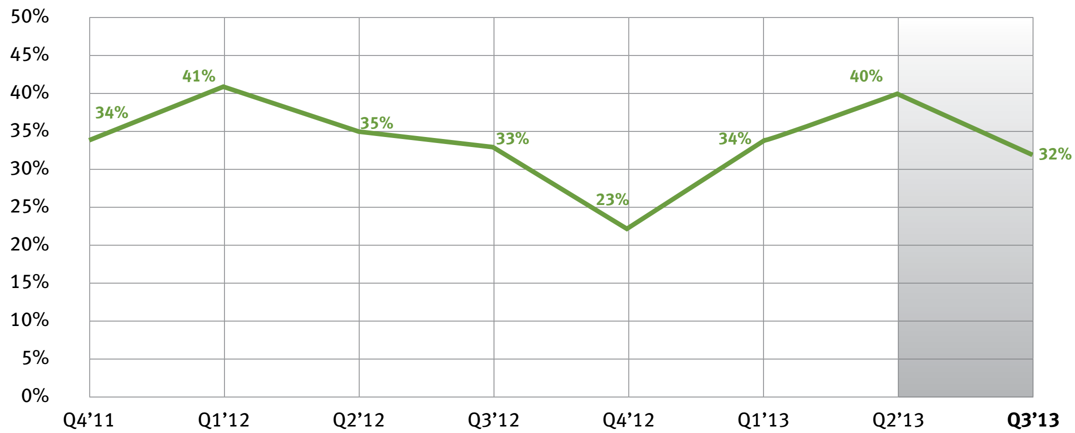


FINANCING ROUND — This quarter's financings broke down by series according to the chart below.

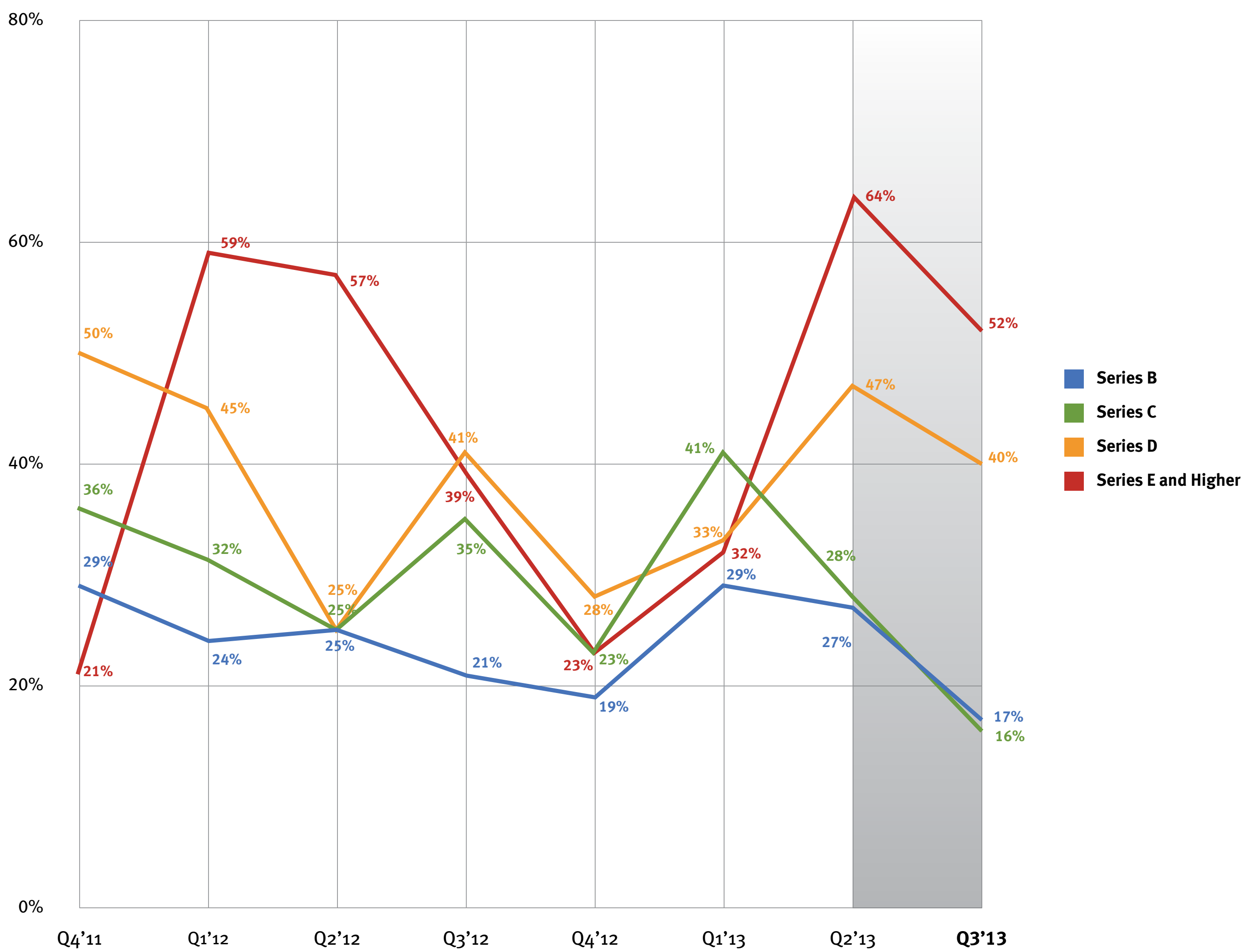
Series	Q4'11	Q1'12	Q2'12	Q3'12	Q4'12	Q1'13	Q2'13	Q3'13
Series A	24%	24%	24%	24%	12%	25%	24%	24%
Series B	24%	18%	17%	24%	31%	20%	24%	23%
Series C	19%	17%	21%	22%	22%	19%	20%	15%
Series D	17%	17%	14%	15%	16%	18%	14%	15%
Series E and Higher	16%	24%	24%	15%	19%	18%	18%	23%

Fenwick & West Data on Legal Terms

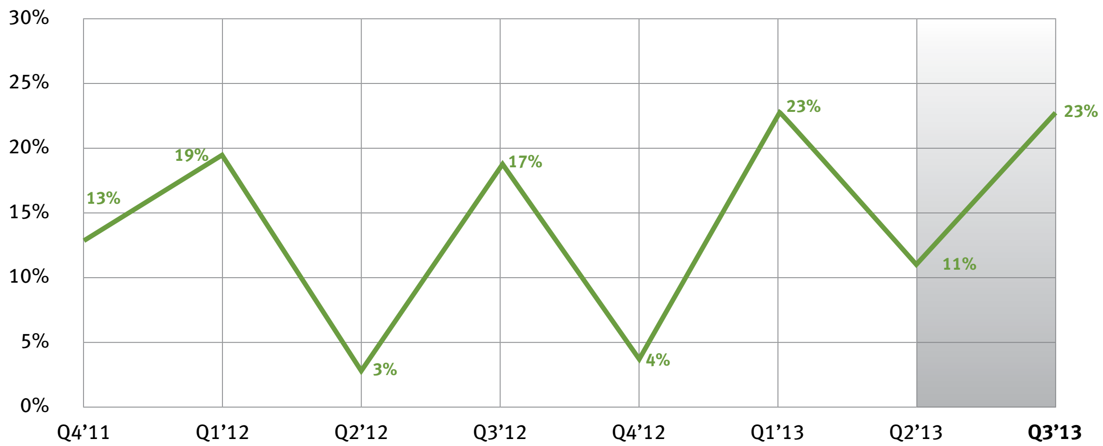
LIQUIDATION PREFERENCE — Senior liquidation preferences were used in the following percentages of financings.



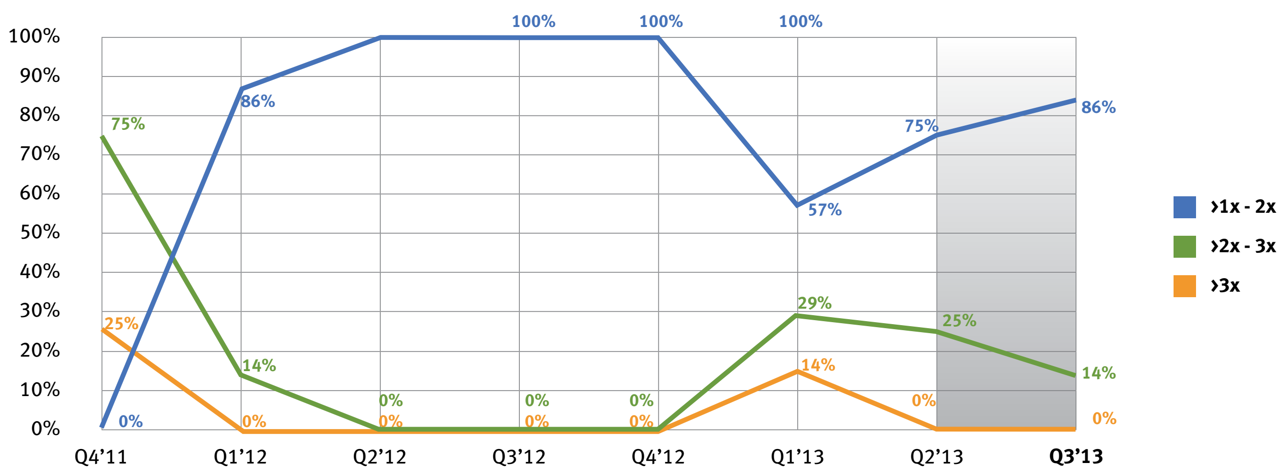
The percentage of senior liquidation preference by series was as follows:



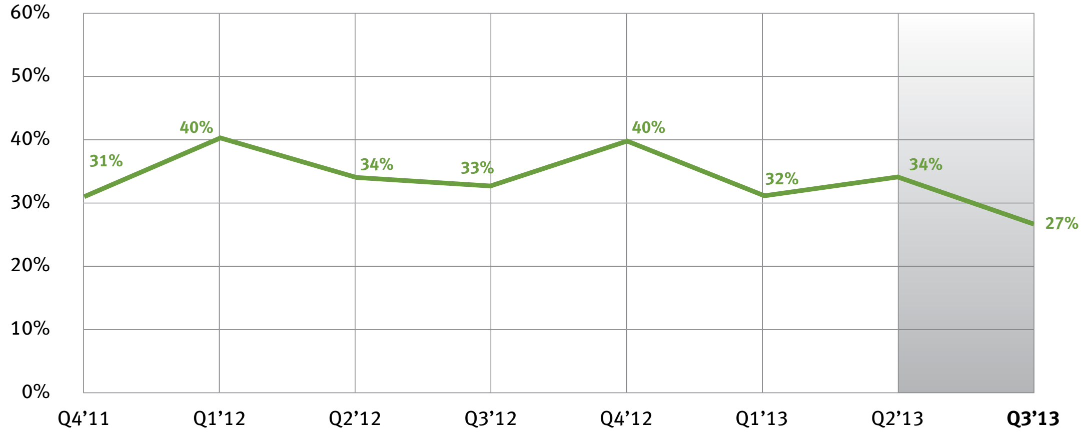
MULTIPLE LIQUIDATION PREFERENCES — The percentage of senior liquidation preferences that were multiple liquidation preferences were as follows:



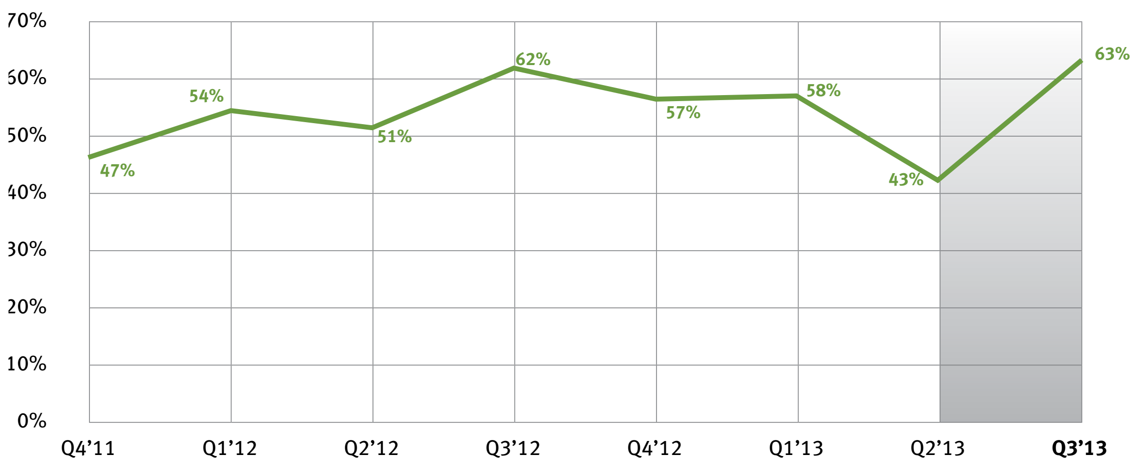
Of the senior liquidation preferences that were a multiple preference, the ranges of the multiples broke down as follows:



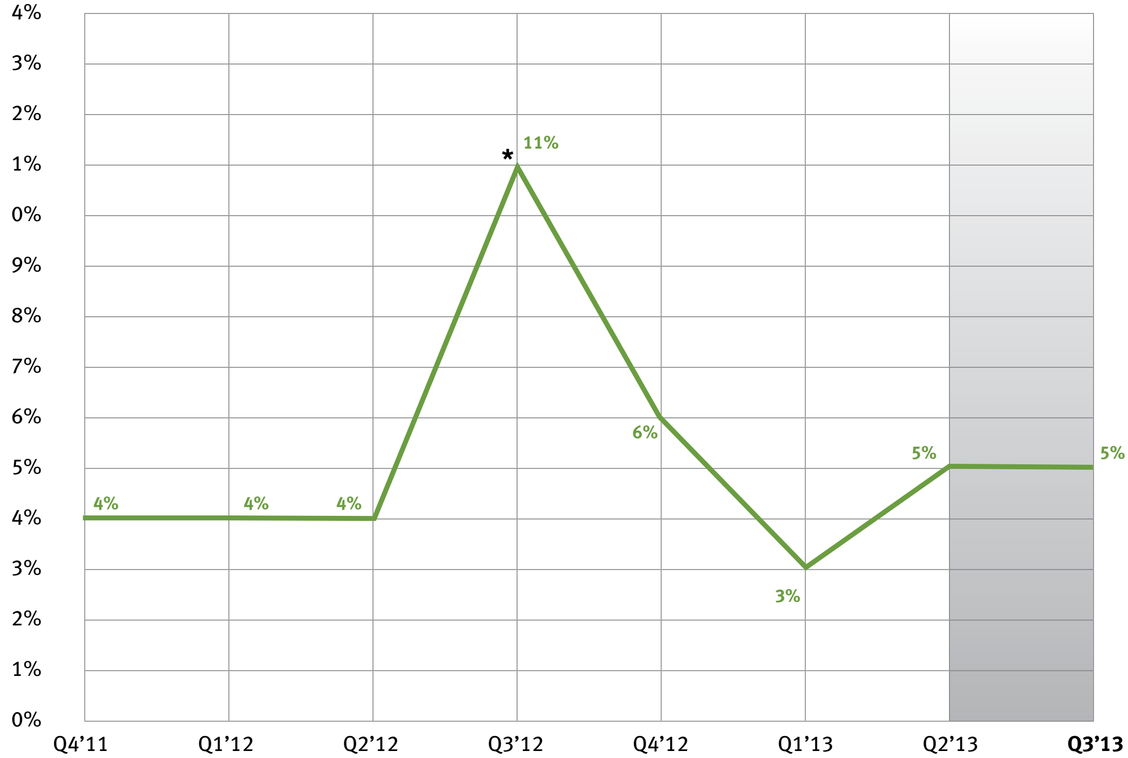
PARTICIPATION IN LIQUIDATION —The percentages of financings that provided for participation were as follows:



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

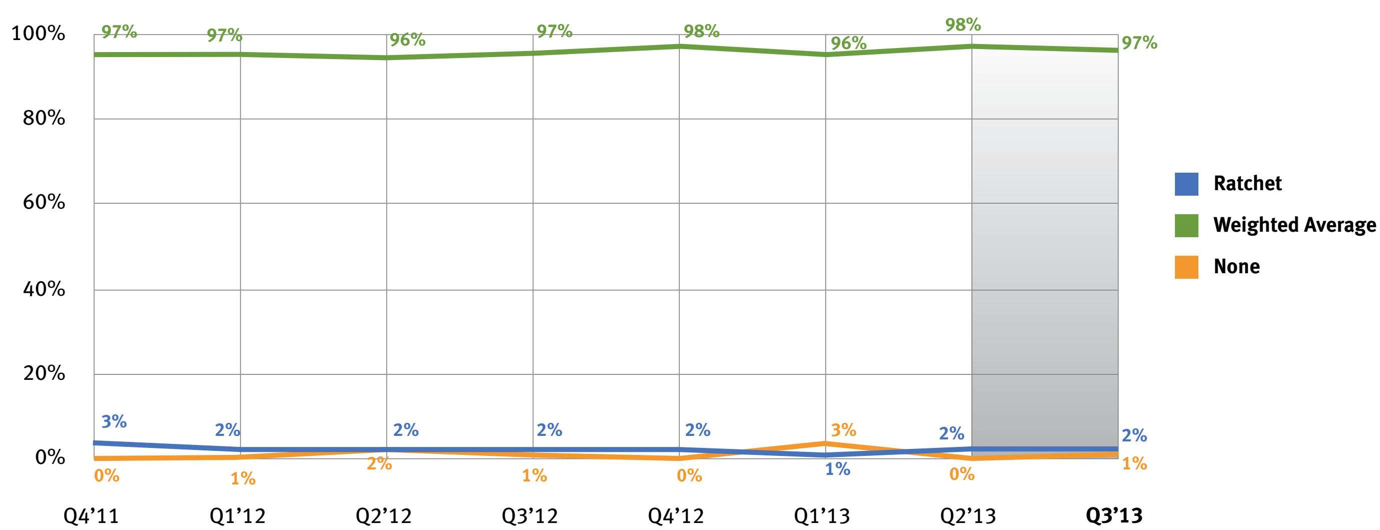


CUMULATIVE DIVIDENDS – Cumulative dividends were provided for in the following percentages of financings:

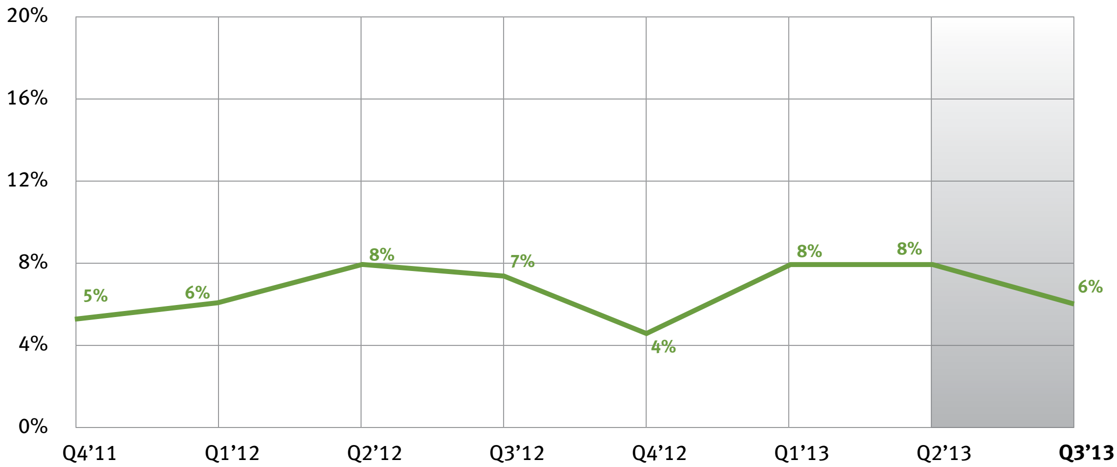


* Note that the use of cumulative dividends increased noticeably in 3Q12. We note that 46% of the financings using cumulative dividends were in the life science industry, and that 38% of the financings (and 33% of the life science financings) using cumulative dividends did not provide for a participating liquidation preference, suggesting that in those financings' cumulative dividends were used as a substitute for participating liquidation preference.

ANTIDILUTION PROVISIONS –The uses of antidilution provisions in the financings were as follows:

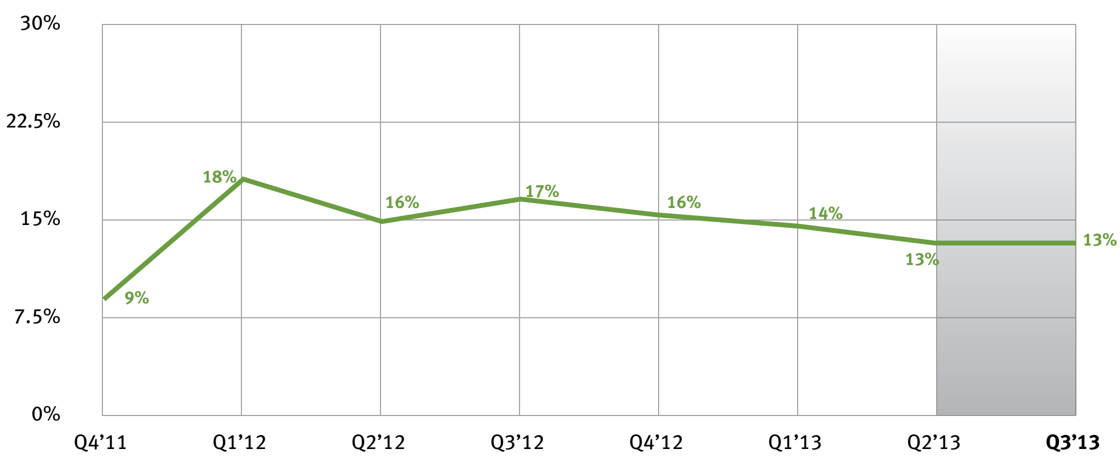


PAY-TO-PLAY PROVISIONS – The percentages of financings having pay-to-play provisions were as follows:

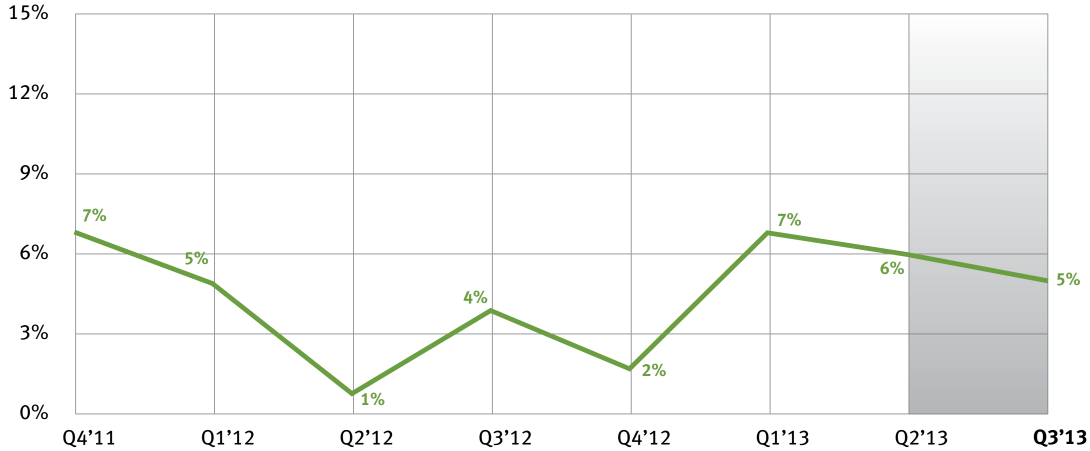


Note that anecdotal evidence indicates that companies are increasingly using contractual "pull up" provisions instead of charter based "pay to play" provisions. These two types of provisions have similar economic effect but are implemented differently. The above information includes some, but likely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

REDEMPTION – The percentages of financings providing for mandatory redemption or redemption at the option of the investor were as follows:



CORPORATE REORGANIZATIONS – The percentages of post-Series A financings involving a corporate reorganization (i.e. reverse splits or conversion of shares into another series or classes of shares) were as follows:



- **Footnote**

[1] When comparing current period results to prior period results based on third party data (e.g., amounts invested by venture capitalists, amount of M&A proceeds, etc.), we use the prior period results initially published by the third party for the period, not the results that have been updated with additional information over time, to provide better comparability with the current period published results. For example, when comparing fourth quarter results to third quarter results, we use the initially published third quarter results, typically provided in October, not the updated results that are typically provided in January of the following year. Such situations are set forth in our report with a parenthetical as to the date the information was initially reported.

- **About our Survey**

The Fenwick & West Venture Capital Survey was first published in the first quarter of 2002 and has been published every quarter since then. Its goal is to provide information to the global entrepreneurial and venture community on the terms of venture financings in Silicon Valley, as well as trends in the overall U.S. venture environment.

The survey is available to all, without charge, by signing up at www.fenwick.com/vcsurvey/sign-up. We are pleased to be a source of information to entrepreneurs, investors, educators, students, journalists and government officials.

The survey consists of two different information sources—(i) our own analysis of deals done in Silicon Valley, including information on both valuations and legal terms, and (ii) an analysis of third party data on overall trends in the U.S. venture environment.

Our analysis of Silicon Valley financings is based on independent data collection performed by our lawyers and paralegals, and is not skewed towards or overly representative of financings in which our firm is involved. We believe that this approach, compared to only reporting on deals handled by a specific firm, provides a more statistically valid and larger dataset.

We aim to publish our survey approximately six weeks after the end of each quarter, to allow time for the major third party sources of information on the nationwide venture environment to publish their results, so that we can analyze and report on the larger trends that might not be apparent in individual reports.

- **Note on Methodology.**

When interpreting the Barometer results please bear in mind that the results reflect the average price increase of companies raising money in a given quarter compared to their prior round of financing, which was in general 12 to 18 months prior. Given that venture capitalists (and their investors) generally look for at least a 20% IRR to justify the risk that they are taking, and that by definition we are not taking into account those companies that were unable to raise a new financing (and that likely resulted in a loss to investors), a Barometer increase in the 40% or so range should be considered average.

We also provide links to third party reports where possible, to provide our readers with more detailed information if desired. In this regard we would like to expressly thank the Venture Capital Journal for providing our readers access to links that would otherwise be behind their "paywall."

- **Disclaimer.**

  The preparation of the information contained herein involves assumptions, compilations and analysis, and there can be no assurance that the information provided herein is error-free. Neither Fenwick & West LLP nor any of its partners, associates, staff or agents shall have any liability for any information contained herein, including any errors or incompleteness. The contents of this report are not intended, and should not be considered, as legal advice or opinion.

- **Contact/Sign Up Information**

  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 view the most recent survey please visit fenwick.com/vcsurvey. To be placed on an email list for future editions of this survey please visit fenwick.com/vcsurvey/sign-up.

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