

# Microcap public biotechs access new pool of VC funding

Venture capital (VC) firm Abingworth Management has invested €33.1 (\$40.6) million in a public German diagnostics firm Epigenomics in a deal known as a VIPE—a venture investment in public equity. The late March offering aimed to help the company build its commercial infrastructure to launch a novel blood-based colon cancer detection kit (*Nat. Biotechnol.* 27, 1066, 2009). This sizeable investment in a company that has already ‘gone public’ is unusual, because VC firms have traditionally focused earlier in the company creation process, funding a portfolio of startups. But with poor historical returns and a lack of current exits—either through a sale to another firm or an initial public offering (IPO)—VC firms are now preferring to invest in more mature, publicly traded companies, the share prices of which have slumped since the Lehman Brothers crash. “There are opportunities in the public markets where biotech as a sector has been beaten up badly on share valuations,” says Jamie Topper, general partner at VC Frazier Healthcare Ventures in Menlo Park, California. “The quality players have been hit along with the dross.”

Some leading VC firms—such as Abingworth, located in London, Venrock of Palo Alto, California, ProQuest, of Princeton, New Jersey as well as Frazier, with offices in Seattle and Menlo Park, California—are now switching their interest away from privately held startups toward these later-stage public firms. It is not entirely a new strategy: private investments in public equity (PIPEs) have been around for years. In a typical PIPE, the private equity firm identifies an undervalued company, invests a small amount for the short term and waits for the share price to recover before exiting at a profit.

The drawback of the PIPE strategy for venture capitalists has been the difficulty of identifying prime candidates. Biotech shares were not always so wildly underpriced as they are now, and most such companies typically need several more financings before their share prices show a worthwhile gain. Under these circumstances, the risk of failure at some intermediate point, such as a disappointment in the clinic, is high. “So the shares of these companies typically traded sideways, or more often down, as events played out,” says David Pinniger of SV Life Sciences Advisers, London, a leading British VC company. This slump was exacerbated as hedge funds preyed on the company stocks, finding them relatively easy targets for short-selling (that is, betting that the price will drop). For these reasons, Pinniger



VC firms are searching for biotech pearls in an undervalued public market.

reckons returns to VC life-science specialists from PIPEs have been very poor so far. “Most are likely to have lost a significant amount of capital over the past five years,” he says

The attractiveness of such investments in public companies is now increasing, though, because the valuations of many early-stage, publicly listed biotech companies are so low and many companies are in dire need of cash. To take advantage of this, several VC groups are reinventing the PIPE as the VIPE (Table 1).

Under a typical VIPE arrangement, a VC syndicate does a very large fundraising—enough to see the company through the critical development phase to proof of concept, or until it reaches a major milestone where there is a significant uptick in valuation, such as partnering or product approval. This could be several years down the line, says Pinniger. At that point, the idea is that venture capitalists will be able to cash in their holdings at perhaps 2.5 to 3 times the amount they originally paid. The profit is amplified because, when they first invested, company stock would have been bought at a discount to the already heavily undervalued market price. “This can provide a lifeline for earlier-stage public biotech companies with high-quality assets,” says Pinniger.

But the capital often comes at a price. “Venture capitalists are able to extract very aggressive terms for these financings, often more or less wiping out the value of investments held by company’s existing investors and perhaps also the company founders,” warns Pinniger.

One VC firm that has aggressively pursued VIPE financings in biotech is Abingworth. “A lot of [investor] money has gone out of the stock market sector consisting of small, risky companies, leaving a lot of them in a very sticky position with inadequate cash reserves,” says Abingworth’s Joe Anderson. “But there are some very compelling development programs in that sector.” Abingworth began its VIPE foray in

## IN brief

### Genzyme partners TJAB

Genzyme of Cambridge, Massachusetts and the Tianjin International Joint Academy of Biotechnology and Medicine (TJAB) in China agreed last month to form a partnership that will bring Genzyme’s products to China. TJAB, co-founded by a public consortium of federal and municipal governments, opened officially in 2009. Its brand-new public biotech platform was built to accelerate the process of biological discovery through to clinical trials. Richard Gregory, Genzyme’s head of research, cites TJAB’s creative thinking and systematic approach as incentives for partnership. From the collaboration, Genzyme hopes to capture innovation from the ground up, while offering TJAB the industrial experience they currently lack. The partnership may also generate future employees for Genzyme and help consolidate the company’s presence in China, says Gregory. Genzyme has invested \$70 million in a major R&D facility in Beijing, the Zhongguancun Life Science Park, and sponsors academic groups across the country. Roger Xie, head of TJAB’s US Operation, said that working with Genzyme “will be a giant step moving forward.” Genzyme may kick-start TJAB’s pipeline by offering several products already in preclinical and clinical development, and Xie expects that many jointly developed therapies will be relevant for patients worldwide. Details of the partnership, including financial incentives, are still under discussion.

Jennifer Rohn

### China’s heparin billionaires

On May 6, Li Li and his wife Li Tan became China’s richest couple when their company, Hepalink Pharmaceutical, in Shenzhen, floated on the Shenzhen Stock Exchange. Although they lost the crown soon after, when stock prices slumped in mid-May, this is the first time the biopharma sector has produced China’s top billionaires. When stocks surged to 148 yuan (\$21.80) per share—the highest on record for a Chinese stock—the Li couple’s 70% ownership was valued at 46.5 billion yuan (\$6.8 billion). Hepalink is China’s largest producer of the blood-thinning heparin, a drug sourced and purified from pig intestines. Analysts commented that the hike in Hepalink’s share price shows that investors are still optimistic about the sector despite the contamination debacle in 2008 that linked over 80 deaths to heparin sourced in China and manufactured by Baxter of Deerfield, Illinois (*Nat. Biotechnol.* 26, 477–478, 2008). Although most Chinese heparin producers have been beset by trouble since then, investors’ enthusiasm for Hepalink possibly reflects the fact that it is currently the only Chinese company approved by both the US Food and Drug Administration and the European Directorate for the Quality of Medicines and HealthCare to export heparin. But Zhaohui Peng, former president of Shenzhen-based SiBiono GeneTech, notes that to maintain their fortune, the Li couple must invest in developing new drugs, because the technological threshold to produce heparin is too low to fight off competitors.

Hepeng Jia