Speaker Notes: C-Suite Networking Dinner (02.26.20)

Bay Area Healthtech & Bioscience Leaders

I. Healthcare Investments and Exits: Hot IPO Market Drives the Healthcare Sector

Silicon Valley Bank: Jonathan Norris, Managing Director, jnorris@svb.com

- Focus of the presentation on Biopharma, and Diagnostics (Dx) and Tools sectors
- Total Healthcare investment dollars were down in 2018 after a record 2018, but still are nearly 50% higher than in 2017
- European investment showed 50% uptick year over year in 2019
- Biopharma investment was slightly down in 2019, after nearly doubling in 2018
- Diagnostics (Dx) and Tools saw the largest decline in 2019 at -20%
- In 2019, about $10.2 Billion raised by VCs to be invested in healthcare
    - There are plenty of other sources of funding available as well, but this is a big amount available for stable, thesis-driven long-term capital
- Continued investment from Crossover Investors (publicly minded investors who are opportunistically investing in venture-backed companies)
- Biopharma
    - Overall investment down by about $1 Billion in 2019
    - Oncology leads in number of deals and total dollars
    - Total dollars declined for Platform, but number of deals remained the same: several Platform deals went public and we saw more Series A investment versus large crossover deals
    - Crossover deal statistics:
        - Over the past 3 years 52% of companies that raised rounds of >$40M have gone public or been acquired
        - In 2017, there were 31 unique deals and 81% of the companies have gone public or been acquired since (only 2 haven't)
        - In 2018, there were 61 unique deals and 48% of the companies have gone public or been acquired since
        - In 2019, there were 45 unique deals and 31% public of the companies have gone public or been acquired since
            - That is a high percentage getting funded by crossovers and going public in the same year
        - This shows positive IPO sentiment
    - Many crossover investors still very active but most have pulled back slightly since 2018
    - Google Ventures is the #2 corporate investor in pure therapeutic investing (not just Biopharma companies using AI or Machine Learning)

    - In 2018 and 2019, aside from Schrodinger and Beam who have performed well post-IPO so far in 2020, highly valued post-money Biopharma companies who went public have not performed very well overall (slightly down post IPO)
- Diagnostics (DX) and Tools
    - Dx tests have staged a comeback from 2019, despite being a difficult sector to raise money in
        - Generally, get acquired for a multiple of revenue, which is not a great exit, but there now is a lot of Series A activity beginning to happen
    - R&D tools experienced a decline in dollars invested
    - Dx test companies and Oncology (liquid biopsy) have garnered the most investor activity
    - Of the highest valued private companies, only Twist and 10x have IPO'd in this sector from 2018-2019, but there are multiple private companies that have post-money valuations over $1 billion
- Healthcare Exits
    - Total Biopharma exit value (M&A and IPO) was $46 Billion in 2019, with Oncology dominating Biopharma IPOs
        - In Private M&A, time from series A to exit was 2.9 years
    - Most companies have step up in value from Crossovers to Mezzanine and from Mezzanine to IPO
    - Diagnostics and Tools exit values were dominated by IPOs in 2019 (much less by M&A)
- Since 2015, 53 IPOs over $1 Billion for VC-Backed Biopharma companies and 26 M&A deals over $1 Billion (7 after going public)
- Of the 20 companies that went public in 2019 and had a market cap of $1 Billion at the end of the year, twelve went public below $1Billion with a median value of $582 Million at IPO but through post-IPO performance built into $B+ market caps.
- Strong average performance from Biopharma IPOs that had a Crossover investor in a late private round
- 2020 Healthcare Outlook
    - Biopharma investment decrease 10-15% but 28-35 IPOs
    - Dx/Tools investment should remain stable and we look for multiple-billion-dollar IPOs/exits in this sector (possibly in 2020)
    - Look for active first half of year push
    - "Exit market better than we've ever seen, even though early investment is lower"

II. Avoiding Common Mistakes in Structuring Compensation Programs & Processes

Compensia: Erik Beucler, Principal, ebeucler@compensia.com

- Use relevant market data and define your compensation philosophy.
    - Should be highly tailored to your company and sub industry because comp data does not translate well across broader industries (Biotech vs Medical Devices)
    - Key factors for choosing comps: Valuation, Revenue, Stage of Life, and what makes your company unique
    - Defining compensation philosophy enables clear communication with Board of Directors and Executive Team, and allows for consistent decision making
- Formalize Your Refresh Program for Equity

    - Lots of variety in strategies in Biotech as opposed to Med Devices
    - Any of the strategies can work as long as they are consistent and communicated in advance to employees and board
    - Avoid dilution protection meaning make sure employee grants are based on current market data (vs. when they initially joined)
- Plan for Your Growth
    - Estimate your share needs for full year
        - Use a bottom up approach
        - Avoids debate at time of grant
        - Ensures pool request is sufficient
- Get the Evergreen Funding Correct at IPO
    - Background
        - Evergreen provision typically provides an auto increase in the available share reserve on the first day of each year for period of 10 years
            - 90% of tech, med device, and biotech/pharma adopt this at IPO
        - The problem is that funding often constrained by a hardwired number of shares rather than using an intended percentage due to financing
        - Companies have been going public with 4% evergreens because it is the norm and then reacting by doing what they need to do to add to them. But they really should be planning for this to happen
- Standardize Severance & Change of Control Arrangements
    - Avoid individually-negotiated arrangements; instead, standardize terms across executives (by level) to reflect market norms and best practices
        - Saves time and energy, results in consistency across management team, avoids surprises and headaches as you transition to a public company, and allows one negotiation instead of multiple
- Build Capabilities to Enable Pay Differentiation
    - Differentiation is increasingly necessary as the company grows but is easier said than done
    - Requirements for successfully executing pay differentiation include:
        - Clear and well communicated compensation philosophy that specifies the compensation tools (base, bonus, etc.)
            - How are different tools used for different levels?
- Build a Compensation Committee calendar
    - Build an annual Compensation Committee calendar with key agendas for each meeting
    - Executive compensation decisions typically require 5 days and companies should aim for 2 to 4 meetings, narrowing the focus each meeting
    - Checklist for compensation committee: 1) Approve peer group, 2) Approve compensation philosophy, 3) Review market data and supporting analytics, 4) Review of management recommendation, 5) Receive Board approval
- Consider Restricted Stock Units (RSUs) before it's too late
    - Consider granting a mix of options + RSUs at larger market cap companies because people don’t perceive as much upside in larger market and later stage companies

        - At pre-commercial biotech companies, stock options remain the most common equity vehicles because people perceive a lot of upside
        - RSUs help with retention when stock prices are volatile and assists with recruitment when candidates have in-the-money options or RSUs at their current employer
        - Also helps avoid necessity for large cash signing bonuses and manage dilution

III. Capital Markets Discussion

PwC: [Daniel Klausner](), MD - Capital Markets Advisory Leader, [daniel.h.klausner@pwc.com]()

- Markets have reset a similar level to the beginning of the year following the sharp decline this week
- In 2019, IPO proceeds hit a 5 year high at $56.2 Billion
    - Most IPOs in Q4 2019 and Q1 2020 were priced within their range
- Medical device companies continue to outperform the broader market due to
    - Resurgence
    - Serial Management Teams
- Most Med Tech and Med Device companies have Dual Track plan (IPO and M&A)
- IPO windows open and close quickly
    - VIX below 20 is good for IPOs
- Early 2020 IPOs have been primarily Pharma & Life Sciences, and Technology.
- Selected recent Biotech IPOs performed above the market
- Selected recent Medical Devices IPO performed above the market
    - All about revenue for these companies
- The themes that are valued most highly in an IPO are: Strong Top Line Growth, Valuation, Predictable Revenue, Experienced Management Team, and Technology
    - Particular interest in high predictability (SaaS type) companies, some Med Tech companies also demonstrated these attributes
- Biotech IPO performance since 2017 by Development Stage
    - 12 companies going public prior to completing the preclinical phase, and the most companies (39) going public with Phase 2 still ongoing.
    - Not many go public in late Development Stages because the outlook for companies are mostly set (goal posts are “in the ground”)
- In 2019, IPO market returned 31% which is very robust
- Underwriter (investment bank) selection
    - Issuers (companies) have lots of leverage to choose investment bankers (using lots of available data)
- Our approach to IB selection: research capability, sector expertise and track record, distribution capability, attention and focus by IB, analyst selection process, syndicate complementarity, and syndicate structure and compensation
- Equity Story Development
    - Biotech: Many written as Industry, Problem, Solution
    - Med Tech could have very SaaS-like KPIs
- Lessons learned: Make sure you are ready to be public, know who you are, raise more capital than you need, timing is everything, and management matters