Evaluate Vantage

January 13, 2017

# Even a $100m series A cannot save the medtech venture climate

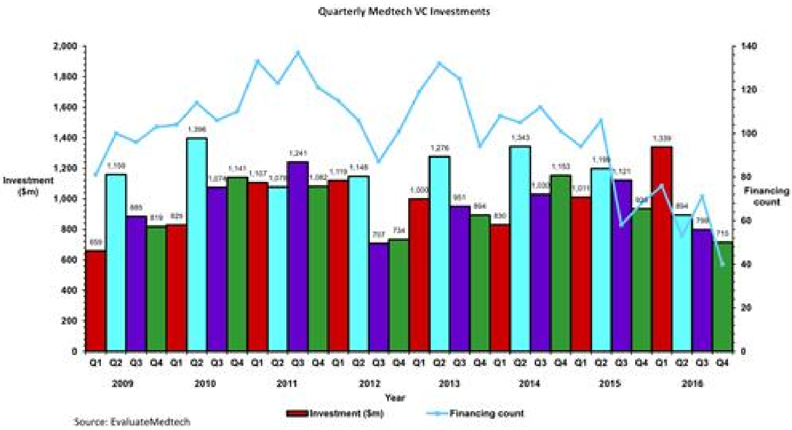
Elizabeth Cairns

Venture funding for medtech companies is getting deeper into an endless winter. While there are some rich rounds, even in the early stages – Grail Bio’s extraordinary $100m series A springs to mind – most companies are struggling to find growth capital.

And with *EP Vantage*’s analysis showing that M&A activity is down, particularly with regard to acquisitions of innovative start-ups, the VC freeze might have begun to affect buyers too. With ever fewer start-ups able to raise money to get off the ground, larger companies in need of new technologies seem already to be finding it harder to identify good takeover targets (see tables below).

And this, of course, will cause a feedback loop; if start-ups cannot easily find buyers there is ever less incentive for VCs to put their money into this sector. Similar trends have been identified in the pharma sector as well (*Chasing ever bigger, ever fewer venture rounds, January 16, 2016*).

The decline in both the number and value of VC rounds raised by device manufacturers is clear, with the fourth quarter of 2016 seeing just 40 deals for a total of $715m. But the average size of these deals has increased once more: from $11.2m in the third quarter to $17.9m in the fourth, aided by Oxford Nanopore’s $126m series I – the first series I the sector has ever seen.

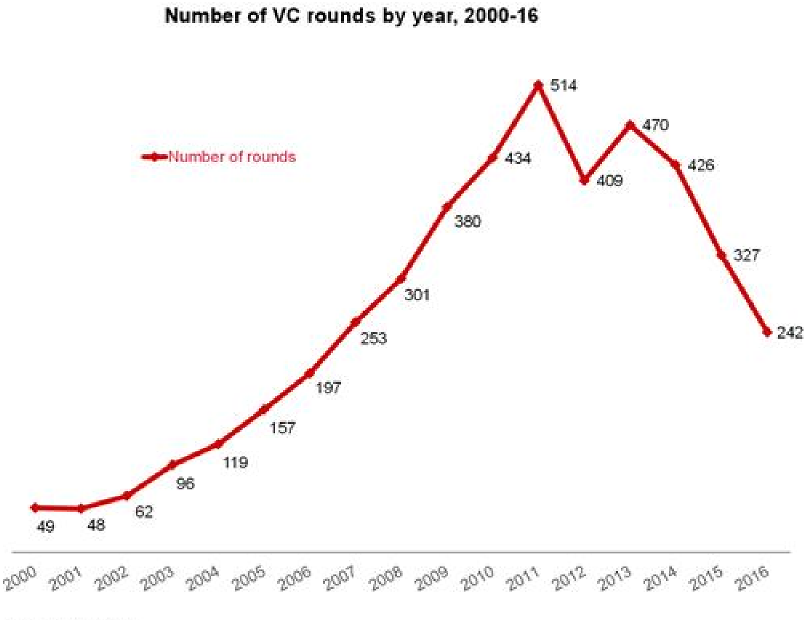



These larger, later rounds are largely responsible for the fact that the average round size has topped $10m for 10 of the last 11 quarters. But one company has bucked this trend. The Illumina spinoff Grail Bio, active in the hot area of high-throughput sequencing and digital health, managed to score part of its funding from two tech billionaires, Bill Gates – or at least the foundation that bears his name – and Amazon’s founder, Jeff Bezos.

In so doing Grail sucked in almost a third of the total series A cash this year (*More medtech venture cash goes into series A rounds, November 30, 2016*). The other top-10 deals were later – the funding obtained by Acufocus and Transmedics, in undisclosed rounds, were their eighth and ninth fund raisings respectively.

| Top 10 rounds of 2016 | | |
|---|---|---|
| **Company** | **Round** | **Investment ($m)** |
| Flatiron Health | Series C | 175.0 |
| Oxford Nanopore Technologies | Series I | 126.0 |
| Guardant Health | Series D | 100.0 |
| Grail Bio | Series A | 100.0 |
| CVRx | Series G | 93.0 |
| Acutus Medical | Series C | 75.0 |
| Acufocus | Undisclosed | 74.9 |
| Heartflow | Series E (second close) | 64.0 |
| Transmedics | Undisclosed | 51.2 |
| Proteus Digital Health | Series H | 50.0 |

Analysed annually, the dropoff in the number of deals is startling. 2016 saw the fewest financings for a decade, and with the intra-quarter fluctuations smoothed out it becomes immediately obvious that since 2013 the decline has been devastatingly swift.




Source: EvaluateMedtech

After the substantial consolidation in the medtech industry in recent years there are fewer acquirers, limiting start-ups' chances of an exit. Caution across the board means that pre-revenue medtechs have small hope of persuading buyers or VCs to part with their cash.

And if fewer early-stage medtechs can raise capital – if fewer venture investors are willing to bet on fledgling companies – this will have a knock-on effect on innovation for years to come. Mid- and large-scale groups will slowly become less able to offer innovative devices, hurting their sales, giving them in turn less cash with which to acquire.

**Strategic**

Perhaps realising this, larger groups are stepping up their corporate VC activity: Johnson & Johnson, GE Healthcare, Qiagen and Fresenius have all made investments this year. And biopharmas are active here too, with companies including Pfizer, Roche, Novartis and Merck backing medtech development, often in the area of diagnostics.

Increased investment from the big players for strategic reasons is good news; it is just a shame that it has been prompted by the dire lack of funding from traditional VCs. And it is clearly not close to making up the shortfall; even with corporate investment the totals are shrinking by the quarter.

With VCs blaming big-cap medtechs for not buying, and the industry leaders insisting that VCs are not adventurous enough with their choice of investments, there seems to be little chance of the sector's troubles lifting in the short term. The sector does not need $100m series A venture deals – it needs $10m series A venture deals. Lots of them.

*To contact the writer of this story email Elizabeth Cairns in London at elizabethc@epvantage.com or follow @LizEPVantage on Twitter*