

## Ariz. investors gather this week to hear entrepreneurs' pitches

by **Andrew Johnson** - Dec. 7, 2008 12:00 AM  
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Job losses in the retail and real-estate sectors have highlighted Arizona's dependence on those boom-and-bust industries.

As business boosters and political leaders brainstorm ways to diversify the state's economy, supporters of technology startups, bioscience firms and other entrepreneurial ventures say increasing financial investments into such companies could help Arizona weather future economic storms.

One of the largest efforts to spark investor interest in local startups happens this week with the kickoff of Invest Southwest.

Organizers of the annual investment conference, now in its 16th year, expect nearly 300 people to attend. The conference takes place Wednesday and Thursday at Four Seasons Resort Scottsdale at Troon North.

Executives of 12 businesses will give a quick "elevator" pitch to investors in hopes of landing money.

Through the years, conference organizers have tried to target different types of investors: venture capitalists, "angels," private-equity firms and others.

The conference currently attracts everyone from hobby investors with an interest in technology to managers with large, institutional funds.

The goal is always the same:

To spur economic development in the state and throughout the Southwest.

"We want these companies to get funded," said Terree Wasley, director of Technopolis, a technology accelerator at Arizona State University that helps run Invest Southwest. "We want them to be creating solid . . . jobs."

Whether a company's participation in Invest Southwest actually will materialize into a round of funding is never guaranteed. Casting an even bigger question mark this year is the recession, which has caused many investors to grow more cautious about funneling money to startups.

Nationally, companies received \$7.1 billion in venture capital in the third quarter, down from \$7.8 billion a year earlier.

In Arizona, venture capitalists invested \$14.5 million in three companies, down from

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\$71.9 million in eight companies a year ago, according to deals disclosed in PricewaterhouseCoopers and the National Venture Capital Association's third-quarter MoneyTree Report .

Some investment firms are insulated to a degree from the economic downturn because they raised their money before the financial crisis exploded.

Still, venture capitalists "are hunkering down some," said Dave Bittner, chairman of Invest Southwest. "They're not immune to what's happening in the macro-economy."

### Growth capital

The dozen presenters at this year's conference were selected from about 80 applicants.

To qualify, a company must be seeking between \$250,000 and \$5 million in capital. The range is appealing to both "angel investors," who invest smaller amounts in early-stage ventures, and venture capitalists, who invest millions of dollars at a time, typically in more advanced companies.

Investors receive an equity stake in the firms with the hope of making a return - often through an initial public offering or merger with another company.

The money is important because it helps startups develop new products, hire employees, market to customers and ramp up sales.

Revenue and employment growth at VC-backed companies traditionally outpaces growth in the overall economy, according to a recent report by the National Venture Capital Association in Arlington, Va.

Specifically, revenue at VC-backed companies grew 11.8 percent, and employment increased 3.6 percent between 2003 and 2006.

By comparison, employment nationally grew by 1.4 percent and company sales rose nationally by 6.5 percent during the same time.

"If you look at the biggest economic drivers in a country or in a state, it's really the health of small businesses," said Brian Smith, a managing director with Menlo Park, Calif.-based VC firm Peninsula Ventures.

Smith, who lives in Mesa, is a member of the screening panel that selected the presenters for this year's Invest Southwest.

One of the benefits of the conference for investors and presenters is that when companies are selected to present, they go through a rigorous grooming process to

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help fine-tune their pitches, Smith said.

The process helps companies more effectively communicate their goals to investors and ensures that investors see only the businesses most worthy of receiving funding, Smith said.

Invest Southwest is particularly important now, supporters say, as Arizona is suffering major job losses in construction and service industries, two of the state's biggest employment sectors.

The conference focuses mostly on emerging technology and bioscience businesses, which experts in economic development say could help Arizona diversify its employment base and create higher paying jobs.

The state lost 37,600 construction jobs and 30,700 service-providing jobs between October 2007 and October 2008. The losses helped nudge Arizona's unemployment rate up from 3.9 percent to 6.1 percent during the same period.

### Downturn effect

Organizers and long-time attendees don't anticipate the current economic crisis casting a black cloud over this year's conference.

It is clear, though, that deal flow has

declined this year.

One contributor to the decline is venture-capital firms are raising less money.

Investment firms typically invest in companies out of funds. It can take a year or more for VC firms to complete fundraising.

Venture-capital firms raised \$8.1 billion in 55 funds in the third quarter, according to the National Venture Capital Association and Thomson Reuters.

That represents a decline of 6 percent from a dollar perspective and a decline of 29 percent in the number of funds.

Whether the contraction will make it any harder for Invest Southwest companies to sell investors on their ideas is unclear.

ASU Technopolis tracks companies after they present at Invest Southwest.

About 40 percent of presenters end up receiving funding after they participate, Technopolis' Wasley said. Since 1992, presenting companies have received more than \$300 million, she said.

The notion that most investors currently are not in a position to finance deals is misleading, according to Rudy Miller, chairman and chief executive officer of

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Scottsdale investment bank and VC firm the Miller Group.

Firms that raised funds before the financial crisis came to a head are still in a position to invest because they have liquidity, he said.

VC firms and individuals also do not invest in companies with the expectation of reaping immediate returns.

"We're not investing for the next nine months," Miller said. "We're investing for the next three or five years."

### Opportunistic plays

Some entrepreneurial ventures are affected more than others by the slowdown in VC investments.

Businesses usually seek money from VCs and angel investors in rounds, starting with smaller amounts of "seed" funding and progressing to larger amounts as they grow.

The number of first-time deals fell 20 percent and the dollar value of such deals dropped 12 percent in the third quarter, according to the most recent MoneyTree Report .

A reason for the drop is first-time rounds are considered more risky for investors; companies that receive such financing

typically are less proven and face more hurdles.

During economic slowdowns, investors often funnel additional rounds of funding to companies they already have invested in to help them forge ahead.

"With our own portfolio companies that we've backed, we're certainly being more conservative with the forecasts that we're projecting . . . to make sure we don't overspend or imprudently burn too much money" Smith said.

Smith and others say bad economic times can result in better investment opportunities. Investors usually face less competition for deals during downturns.

In 2007, Peninsula finished raising a \$75 million fund, from which it invested in three businesses last year and five this year.

Smith expects Peninsula, which invests in information-technology businesses, will make three or four more investments from the same fund next year.

### A mix of companies

Not all investors are shying from first-time deals.

Epic Ventures, a Salt Lake City-based firm

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that invests primarily in early-stage companies, has continued doing first-time deals this year.

"We're still actively looking at deals and put down some term sheets recently," said Stephanie Spong, a principal in Epic's Santa Fe office and member of the Invest Southwest selection panel.

"We did more investing in this past year than in recent years because we had money."

Epic recently completed raising its fourth fund. Spong would not disclose how big the fund is, but said Epic has invested \$300 million in companies during the firm's 14-year history.

Investing in fledgling companies that still have months of product development ahead of them is a strategic approach now because such firms are not at the point of having to contend with a crummy sales environment, she said.

"Where it's tricky time right now are with the companies where maybe they're just on the verge of hitting their revenue ramp-up," Spong said.

One of Invest Southwest's appeals is the diversity of the presenters, she said.

This year's firms come primarily from the

technology and life-science arenas, but they're seeking amounts of money that appeal to a variety of investors.

"We try to look at a mix of . . . angel deals and venture-capital deals," Wasley said.

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