

VCS: Signs 'encouraging' for MN

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STAFF WRITER

Minnesota venture capitalists aren't partying like it's 1999, but they're certainly in a better mood than they were in 2010.

Twin Cities VCs say their industry is settling into a new "equilibrium" following a boom-and-bust cycle that left many startups struggling to raise cash.

The investors spoke at a panel discussion hosted by The Collaborative. The *Minneapolis/St. Paul Business Journal* sat in on the conversation, which was moderated by Collaborative CEO Dan Carr.

Venture-capital investment in Minnesota companies fell to a record low in 2010, slipping to \$147 million for the year. However,

the amount of capital raised by the state's startups rose to \$58 million in the first quarter of 2011, up from \$38 million in the fourth quarter of 2010. The uptick could indicate a



Carr

nascent recovery, though challenges remain, investors said.

"Minnesota is showing some early encouraging signs," said Michael Gorman, managing director at Split Rock Partners, an Eden Prairie-based venture-capital firm. For instance, venture-capital investment was spread across several industries in the first quarter. Often, medical-technology companies win more than half of funds raised in a given quarter. "We're seeing a little bit more diversification, which portends a more stable and healthier mix for Minnesota long term."

Overall, Minnesota is more reliant on its historically strong med-tech sector than other states. In 2010, 60 percent of venture capital invested in Minnesota went to med-tech companies, compared to 13 percent nationally, said Buzz Benson, managing director at SightLine Partners, a Minneapolis-based venture firm that invests in medical device and health care companies. However, med-tech startups have struggled in recent years due to regulatory challenges and other hurdles.

It will take time for the sector to recover, Benson said. "The med-tech industry has really suffered. The rebound is a lot stronger on the IT side. It's still going to be a couple of rough years on the med-tech side for funding early-stage companies and even later-stage companies."



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VC ROUNDTABLE PANELISTS

Buzz Benson (top left), managing director, SightLine Partners, a venture-capital firm that invests in medical-technology and health care companies

Ed Spencer Jr. (top right), chairman and founder, Affinity Capital Management, a venture-capital firm that invests in health care and med-tech firms

Vance Opperman (upper right corner), CEO, Key Investment Inc., an investment firm that backs early-stage companies, real estate and publishing businesses

Joy Lindsay (right) president and co-founder, StarTec Investments, a venture-capital firm that invests in early-stage companies

Michael Gorman (lower right), managing director, Split Rock Partners, a venture-capital firm with \$1 billion in capital under management

Dan Carr (moderator), CEO, The Collaborative, an organization that hosts a range of events for entrepreneurs and investors

However, mergers and acquisitions activity in med-tech is picking up, which could help, he said.

Many venture capitalists nationwide are particularly bullish on Internet and software startups these days, especially given the success of companies such as Groupon Inc. and Facebook. Minnesota could become a significant player in that market with just one prominent success story, said Gorman, who focuses on investments in software and Internet-services companies. He cited the success of Chicago-based daily deal site Groupon. That company's rise has attracted both significant tech talent and investment to Chicago.

"That could be a transformative event for Chicago in the same way Earl Bakken and Medtronic was here," he said.

"Minnesota has a very deep software and engineering community. It's an under-appreciated asset in this state," he added.

Companies that want to become that next big success story still face challenges, however. For instance, it's difficult for many young startups to find seed funding in Minnesota, said Joy Lindsay, president and co-founder at Bloomington-based StarTec Investments, which backs early-stage

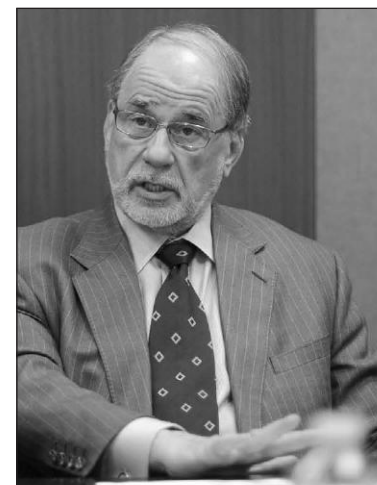
companies. "The smaller venture funds are no longer active. Those groups have been replaced by angel funds or individual angels, which makes it harder for entrepreneurs to actually find those people. You have to be a little more aggressive in finding angel investors."

The angel-investor tax credit program approved by the Legislature last year helped startups attract funds. However, the challenge will be whether those firms can grow to a point where they can raise more money or no longer need outside capital.

"Sixty-seven companies got funded, which is great," she said. "The questions I have are: What happens next? Can angel investors continue to fund those to the point where they are attractive to a venture fund? Sixty-seven is too many to take through the venture funding process."

Investors agree that there are plenty of enthusiastic, talented entrepreneurs in Minnesota.

"I think entrepreneurship is on the rise again, at least from what we've seen," said Vance Opperman, CEO of Key Investment, a firm that invests in a wider range of startups. He's continued to see companies in a variety of industries approach him for investment.



Overall, venture-capital investment is unlikely to reach historic highs any time soon, but investors say it is returning to a reasonable, sustainable level.

"We're moving back into a very healthy environment," said Ed Spencer, chairman and founder of Minneapolis-based Affinity Capital Management, a venture-capital firm that invests in health care and med-tech firms.