

Enterprise

Overview:

Canadian VC Activity Rebounds in Q3

Overall Capital Flows

After two straight quarters of decline, activity in Canada's venture capital industry rose between July and September. At \$361 million, capital invested was up by 52% from the \$238 million disbursed in Q2. In addition, a total of 191 Canadian companies received financing in the third quarter, which approximates the 196 firms of three months prior.

Despite the quarter-over-quarter increase, capital flows continue to be significantly lower than in the corresponding quarter of 2002, when \$563 million was invested in 216 companies. Nonetheless, it appears that the steady declines in Canadian industry activity may have stopped.

By comparison, activity in American VC industry reflected stable, if also historically low levels. After seeing capital invested rise three months ago (for first time since 2000) to \$US4.6

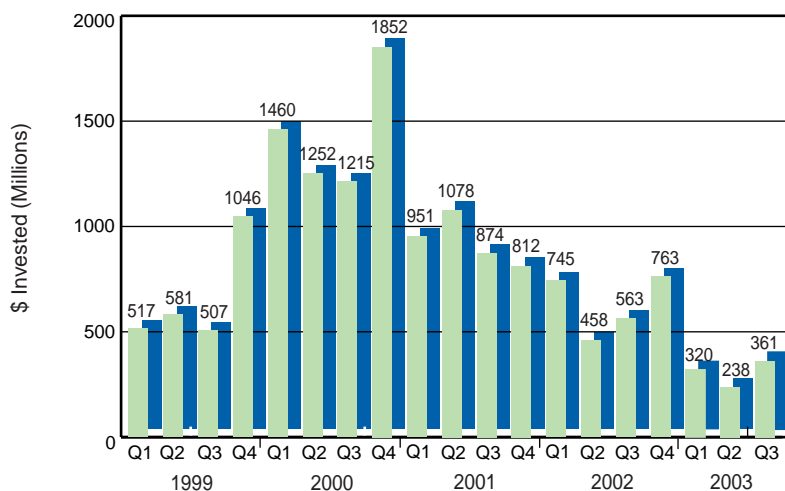
billion, US levels dropped modestly in Q3 to \$US4.2 billion. According to Thomson Venture Economics, there was also a dip in the number of companies financed south-of-the-border, from 706 in the previous quarter to 667.

A key factor in improved Canadian capital flows in Q3 was larger transaction sizes. At close to a dozen, there were more financings sized \$10 million-plus this time, as compared to the second quarter. Consequently, the largest 10 deals in Q3 2003 captured one-third of all disbursements. This share is still shy of Q3 2002, however – when mega-deals of over \$20 million were still prevalent – and the largest 10 deals took nearly 40% of the aggregate.

A higher number of large deals ensured that average company infusions went up to \$1.9 million in the third quarter, as compared to \$1.2 million between April and June. However, 2003 levels remain tepid when viewed against averages

(continued on page 2)

Quarterly Investment Activity
By Canadian Venture Capital Industry



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From the President

This is my first letter to the membership and let me take this opportunity to say how honoured I am to be elected President of the CVCA. I look forward to leading the CVCA in building the industry's stature, here in Canada and abroad.



I want to congratulate the previous President, Brad Ashley, on the tremendous work he has done over the past year in building the CVCA. He leaves a very sound organization, with membership at an all time high of 850 and a very strong financial position.

I would like to welcome Richard Rémillard as the new Executive Director of the CVCA. Richard will work with Kathryn Ryan and Lauren Linton to raise the profile of venture capital and private equity in Canada, lobby governments on issues of importance to the CVCA, and assist the committees of the CVCA board to pursue their mandates. Richard's appointment reflects the maturing of the organization and of the venture capital and private equity asset class in Canada.

I would also like to welcome the new CVCA board of directors. As usual, we have a very enthusiastic and committed group and I look forward to working with all board members during the upcoming year.

The third quarter report on venture capital activity in Canada has just been released and is summarized in this newsletter. While there was an increase in investment activity from Q2 to Q3, activity this year is still significantly less than last year. An optimistic view of the quarter over quarter increase is that the decline has slowed or stopped and this may indicate that we are at, or near, the trough of investment activity—this would mirror the U.S. experience where investment activity seems to have stabilized during the past few quarters. Anecdotal evidence in both countries seems to indicate increased deal activity and so hopefully we will see an improved environment in 2004.

The past few years have been difficult ones for venture capital and private equity and the initiatives of the CVCA in 2004 are focused on expanding awareness by investors of the inherent and long term, attractions of the

(continued on page 3)

New AdVENTURES

■ **Robin Louis**, President of Ventures West Management Inc., has been appointed the new President of the **CVCA**. Robin can be reached at 604-891-3260 or rlouis@ventureswest.com.

■ **Richard Rémillard** has been appointed Executive Director of the **CVCA**. Richard may be reached at 613-744-8969 rremillard@cvca.ca.

■ **Donna Takacs** of the **Canadian Medical Discoveries Fund Inc.** has left CMDF to pursue a new career opportunity. **Paul Farrell** has joined the CMDF team as Vice President, Marketing. Paul will assume all responsibilities previously held by Donna. Paul can be contacted at 416-213-4682 or pfarrell@cmdf.com.

■ **Andrew Treble** has recently joined **Export Development Canada (EDC)**. His new responsibilities include deal origination and structuring with the EDC Equity Team. Andrew can be reached at 613-598-3090 or atreble@edc.ca.

■ **Joseph Regan** joined **Growthworks (WVIS) Ltd.** As Vice President, Investments. His responsibilities include the life sciences portfolio. Joseph can be

reached at 416-934-7731 or joseph.regan@growthworks.ca.

■ **Alyson Soko** has recently joined **Heidrick & Struggles** as Partner. Alyson will continue to conduct executive searches for venture-backed technology companies. Alyson can be reached at 416-361-4720 or asoko@heidrick.com.

■ **Claude Miron** and **Samuel Duboc** announced the launch of **InVivo Ventures**. This initiative, supported by EdgeStone Capital Partners, will see Claude Miron, formerly a partner at Edgestone, join InVivo Ventures as its President and Managing Partner. Claude can be reached at 514-697-3175.

■ **Tom Gunn** is leaving his job as chief investment strategist at the **Ontario Municipal Employees Retirement System (OMERS)** after more than 7 years picking assets for the country's third-largest pension fund.

■ **Mike Reynolds** has recently become Associate at **PENTOR Alliance Corporation**. Mike will be responsible for M&A deal structuring. Mike can be reached at 514-748-8400 or mreynolds@pentor.com.

■ **TD Capital**, the 35-year-old private equity arm of Toronto-Dominion Bank, has said farewell to president **Natalie**

Townsend. The bank's head of wealth management, TD executive vice-president **Robert MacLellan**, took over her responsibilities.

■ **Phil Walton** has retired from KPMG Corporate Finance to establish **Delta Capital Consultants** and will continue to assist small and medium sized businesses arrange capital for expansion, acquisitions and refinancing. Phil may be reached at 416-480-9813 phil.walton@sympatico.ca.

■ On September 8th, 2003, **Gregory Phipps**, who worked with BDC Venture Capital for six years, most recently in the IT sector team, has moved to **Technology Seed Investments (TSI)**, as Director under the leadership of Robert Inglese, VP, TSI. Greg will be responsible for origination and management of seed stage technology opportunities in Eastern Canada, and, as a generalist investor, will consider deals across the "technology" spectrum." Greg may be reached at 902-426-7868 or gregory.phipps@bdc.ca.

■ **Jamie Adam** has been named Vice-President, **Investments of the Return on Innovation (ROI) Fund**. Jamie may be reached at 905-330-0569 or jadam@roifund.com.

Overview *(continued from page 1)*

recorded in 2002 (\$3.7 million) and 2001 (\$5.0 million).

Downward pressure on capital flows continues to be exerted by the industry's focus on follow-on transactions, as many portfolio firms absorb VC resources in smaller increments. Follow-ons consumed 71% of total disbursements in Q3.

Sector Flows

Computer software firms pulled ahead of life sciences in the third quarter, as the Canadian industry disbursed \$77 million to 30 companies – including Quadrus Financial Technologies and Timespring Software Corporation – up by 34% from the \$57 million registered three months earlier. As a result, the sector garnered 21% of total dollars invested.

Other IT sectors also grew in VC industry esteem in Q3. For instance, \$66 million went to DFT Microsystems, R/D Tech and 22 other companies in the electronics, hardware and semiconductors field, up from \$20 million in Q2. Deals behind Critical Telecom and Intelligent Photonics Control Corporation also helped to restore the fortunes of communications, which captured \$53 million, while CollectiveBid Systems, GotMarketing.com and 11 other Internet firms took \$26 million.

Between January and June, life sciences racked up close to one-quarter of all dollars invested by the industry. This share dropped in the third quarter, as 28 firms secured \$64 million, or 18% of the aggregate, despite some key financings, including those for

LymphoSign, Medicago and OncoGenex Technologies.

The current market situation favours traditional sectors, something that was demonstrated again in Q3 with their \$68 million invested, or 19% overall. Joseph Ribkoff and other firms in consumer products and services obtained most of this cash.

Foreign Activity in Canada

The Canadian activity of US and other foreign sources of VC was also up in the third quarter, a trend that is linked with growth in IT investment. Foreign capital flows grew to \$64 million, up from \$25 million in the second quarter. Consequently, non-residents accounted for 18% of dollars invested, suggesting that American funds remain alert and responsive to attractive deal opportunities in Canada.

LSVCCs once again deployed the most resources overall, with \$92 million, or one-quarter of the total. Other Canadian industry players also loosened the restraints. Perhaps most telling was the increase in private LP disbursements, which was up by 70%, from \$33 million in Q2 to \$57 million in Q3. At \$61 million, institutional capital invested was also more robust, as was the activity of government funds with \$48 million.

Early stage deals sustained their historic high in terms of industry preferences, with 91 companies and \$172 million, or close to half of all disbursements (48%). However, it was expansion transactions that gained the most ground in July-September, as 90 firms

secured \$182 million, up by 74% from \$105 million in the second quarter.

Regional Breakdown

Quebec continued to reflect the bulk of VC-backed firms, which totaled 107, or 56% nationwide, and also took 39% of industry resources, or \$141 million. Ontario had much more momentum in Q3, seen in 40 companies and \$153 million, up from \$90 million in Q2, and 42% of dollars invested. Activity was also up on a quarter-over-quarter basis in other regions as well, particularly in BC and Atlantic Canada.

Fund-Raising

While Canadian industry deal activity is improving as the year progresses, the same cannot be said of fund-raising. In the first nine months, a total of \$1.3 billion was added to industry stocks, \$150 million of which was raised in Q3 – over 80% of which came from LSVCCs. At this pace, new commitments to venture funds are not expected to match the \$3.2 billion achieved by the end of last year.

Nonetheless, numerous private LPs are currently in fund-raising mode and should be in a position to announce final closings soon. These include new initiatives involving Canadian and US VC groups – such as RBC Technology Ventures and Milestone Medica Corporation in partnership with VIMAC Ventures LLC and BTG Ventures, as well as Primaxis Technology Ventures in partnership with Draper Fisher Jurvetson.

NEW Funds

■ The **BUSINESS DEVELOPMENT BANK OF CANADA (BDC)** and the **CAISSE DE DÉPÔT ET PLACE-MENT DU QUÉBEC (CAISSE)** have concluded an alliance to increase the amount of financing available to Canada's small – and medium-sized enterprises (SMEs) and support their growth. For further information, please contact Lise Beauchemin at 514-283-7929 or visit www.cdpcapital.com.

■ **CAI CAPITAL MANAGEMENT CO.** and its related companies ("CAI") announced the final closing of CAI Capital Partners and Company III, L.P. and CAI Partners and Company III, L.P. (together "CIA III"), a \$375 million investment fund targeted at private equity investment opportunities in Canada and the United States. For more information, please contact Manfred Yu at 416-306-9893 or visit www.caifunds.com.

■ **CI FUND MANAGEMENT INC. (CI)** announced that it has entered into an agreement to acquire **SKYLON CAPITAL CORP. (SKYLON)**, manager of the VentureLink Group of Funds and a series of retail structured products. For further information, please contact William Holland at 416-364-1145 or visit www.cifunds.com.

■ The **CPP INVESTMENT BOARD** has increased its commitment to two existing private equity partners. An additional \$100 million to the Kensington Capital Partners Limited, of which \$50 million has been committed for the Canadian buyout "fund of funds" and \$50 million to a related fund that will co-invest directly in private companies located primarily in Canada. The CPP Investment Board's total commitment to Kensington Capital Partners Limited is now \$200 million. For more information, please contact John Cappelletti at 416-868-0308 or visit www.cppib.ca.

■ **DRAPER FISHER JURVETSON**, a leading U.S. venture capital firm, pioneering seed stage technology venture capital, announced that they are opening a Toronto-based affiliate office in partnership with **PRIMAXIS**. Aiming to invest US\$100 million in Canadian high-tech companies. For more information, please contact Ilse Treurnicht at 416-974-6840 or www.primaxis.com.

■ The launch of **INVIVO VENTURES** will be set up as a new private and independent venture capital group focusing on life sciences, medical technologies and health care information technology investing pre-

dominantly in Canadian companies. The Fund will offer a unique opportunity for investors to take part in the highly attractive Canadian life sciences sector. For more information, please contact Claude Miron at 514-697-3175.

■ Penfund announces the closing of **PENFUND MEZZANINE FUND II** at the \$106 million level. This fund will provide equity and mezzanine capital in the \$3 - 10 million size range to established Canadian businesses. For more information, please contact John Bradlow at 416-645-3799 or Barry Yontef at 416-645-3800.

■ **PRIVEQ CAPITAL FUNDS** has begun raising its third fund, **PRIVEQ III Limited Partnership**, which will continue to focus on providing equity capital for expansion and buy-out transactions of profitable niche manufacturing and niche service businesses. Target size of the new fund is \$50 - \$100 million. For further information, please contact Brad Ashley, Managing Partner at 416-447-3330 or ashley@priveq.ca.

■ Leading Quebec and Canadian financiers of the life sciences sector, the **SOLIDARITY FUND QFL** and **MDS CAPITAL** have concluded a strategic alliance to provide access to approximately \$200 million of new capital to support life sciences companies at critical stages of their development, including at the second and third rounds of financing. This association consists of independent entities that will work to provide complementary financing. For more information, please contact Greg Gubitz at 416-213-4665 or ggubitz@mdsintl.com.

■ **TECHNOLOGY INVESTMENTS MANAGEMENT CORPORATION (TIMCO)**, Manager of Canadian Science and Technology Growth Fund and **CAPITAL ALLIANCE VENTURES INC. (CAMI)**, announced their amalgamation. The merged company has changed its name to **FULLARTON CAPITAL CORPORATION**. Fullarton Capital will remain at its locations in London and Ottawa. For more information, please contact Susan Smedley at 519-858-1488 X247 or visit www.fullartoncapital.com.

■ **VIMAC Ventures LLC**, RBC Technology Ventures Inc., and BTG announced the commencement of **VIMAC MILESTONE MEDICA FUND (VMM)**, an early stage life sciences fund. VMM is the latest in VIMAC Ventures' Boston-based family of funds and has offices in Boston and Montreal. For more information, please contact Debra Berliner Barda at 212-725-4500 or visit www.vimac.com.

■ **BDC Technology Seed Investments** announces the commencement of **TECHNOLOGY SEED INVESTMENTS GROUP**, an early stage \$80 million fund which invests in Telecom, IT, Advanced Technology and Biotech. For more information contact Gregory Phipps at 902-426-7868 or gregory.phipps@bdc.ca

From the President

(continued from page 1)

asset class and removing barriers to investment. It is critical that these long term attractions are well understood so that we do not fall into several years of malaise such as the years that followed the previous venture capital boom in the late 1980s.

I am heartened by emerging positive signs both in the wider economy and in the venture capital and private equity industry itself. And I am cautiously optimistic that we will emerge from the recent very challenging period stronger than before and that a prolonged period of weakness comparable to that of a decade ago can be avoided. The CVCA is undertaking a number of programs in 2004 help build the foundation for growth of the industry in the coming years:

- *Information* – to increase the amount, quality and timeliness of information available on the industry to levels comparable to that which is available in other countries
- *Institutional investment* – to increase the number of organizations, both in Canada and elsewhere, that will seriously consider investment in Canadian venture capital and private equity
- *Marketing* – to ensure that investors, governments and all other interested parties understand the potential for excellent long term returns and also understand why this asset class is important to innovation and building the economy
- *Tax changes* – to remove impediments to investment
- *Professional development* – to build the strength of the industry
- *Conference* – the 2004 conference will be held in Calgary in May and is always a major focus for the industry

There will also be a major effort to ensure that the association is active and visible in all the major centers of the country and is well connected to angel investors, entrepreneurs and all others who have stakes in the success of new startup enterprises.

The year promises to be a very challenging and exciting one. I look forward to working with the CVCA and to meeting as many of the association's members as possible at one of our many networking and educational events taking place across the country throughout the year.

Best wishes for a safe and happy holiday season, and a successful 2004.



Robin Louis,
President, CVCA

Events Calendar

CVCA Events

- Wednesday, November 19, 2003 – Toronto
New Members' Reception (Members Only)
Fig Leaf Ristorante, 5:00 p.m. to 7:00 p.m.
25 Toronto Street, Toronto, Main Floor
- Wednesday, November 26, 2003 – Toronto*
Professional Development Seminar
'Value-Added Boards'
TSE Conference Centre, 1:00 p.m. to 6:00 p.m.
130 King Street West, Toronto, Main Floor
- Wednesday, December 3, 2003 – Ottawa
Ottawa Networking Reception,
5:00 p.m. to 7:00 p.m.
Restaurant 18, Ottawa
- Wednesday, January 21, 2004 – Vancouver
Vancouver Networking Reception,
5:00 p.m. to 7:00 p.m.
Venue to be confirmed
- Wednesday, February 25, 2004 – Toronto*
Professional Development Seminar
"Management Assessment Techniques II"
Metro Toronto Convention Centre,
North Building, Room 101

- Tuesday, April 13, 2004 – Toronto*
Professional Development Seminar
TSE Conference Centre, 1:00 p.m. to 6:00 p.m.
130 King Street West, Toronto, Main Floor
 - May 26-28, 2004 – Calgary, Alberta
Annual Venture Capital & Private Equity Conference 2004
Canada's premiere Venture Capital and Private Equity Conference
Hyatt Regency Calgary
 - Wednesday, August 25, 2004
Markham, Ontario
2004 Golf Classic
Angus Glen Golf Club
- * CVCA PD EVENTS WILL BE VIDEO
CONFERENCED INTO HALIFAX, MONTREAL,
OTTAWA, CALGARY AND VANCOUVER.

To register for CVCA events, please visit the events page of our web site at www.cvca.ca, or e-mail your contact info and questions to cvca@cvca.ca

Industry Events

- January 27 & 28, 2004 – London, U.K.
Institutional Investors Private Equity Summit
Visit www.euromoneyseminars.com
- March 3 & 4, 2004 – Toronto
Venture Fair 2004
Hosted by Toronto Venture Group, VentureFair 2004 showcases emerging growth companies. Visit www.venturefair.com
- May 3 & 4, 2004 – Toronto
IT Financing Forum East
Canada's leading IT investors and the CEOs of Canada's hottest emerging IT companies get together and talk business during this fundraising showcase.
Visit www.financingforum.com

First Inaugural Golf Classic – Huge Success!

On behalf of the Golf Committee, I would like to thank all of those who made our First Inaugural CVCA Golf Classic held at Copper Creek on August 27 a very successful event. These include the sponsors, the prize donors and the golfers among others. We sold out both the sponsorships and the golfing slots very early, contributing to a solid financial performance for the tournament. As a result, we were able to donate \$5,000 to the Juvenile Diabetes Association on behalf of Aird & Berlis, LLP, our sponsorship winner. The weather was excellent and from all reports both the course and the overall

tournament were very well received by the golfers and sponsors.

David Merry provided some comic relief for the golfers at the dinner, as well as doing duty as the golf pro on the course.

I would like to take this opportunity to remind you to put August 25, 2004 in your calendar now, so you don't miss the 2004 CVCA Golf Classic as we anticipate it will sell out quickly and will be as much or more fun than 2003!

Doug Moore
Co-Chair, Golf Committee



Winners' Circle

CVCA's 5th Annual Deal of the Year Award

The CVCA is pleased to announce **Brightspark Ventures** as the recipient of the CVCA's 5th Annual 'Deal of the Year Award'.

Established in 1998, the purpose of CVCA's 'Deal of the Year Award' competition is to promote, highlight and celebrate the achievements of venture-backed Canadian companies. The selection process focuses on firms with the most significant return during the last twelve months ending June 30, 2003.



Brightspark Ventures won this year's award for its investment in Think Dynamics. The investment in 2001 generated a return of 163% when IBM acquired Think Dynamics in May 2003. This represented an investment multiple of 8.2.

Tony Davis, co-founder and Managing Partner of Brightspark Ventures, accepted the honour at the CVCA's AGM Dinner in Toronto on Tuesday, September 16, 2003.



Questions, comments and contributions to the **Enterprise** are welcome!
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