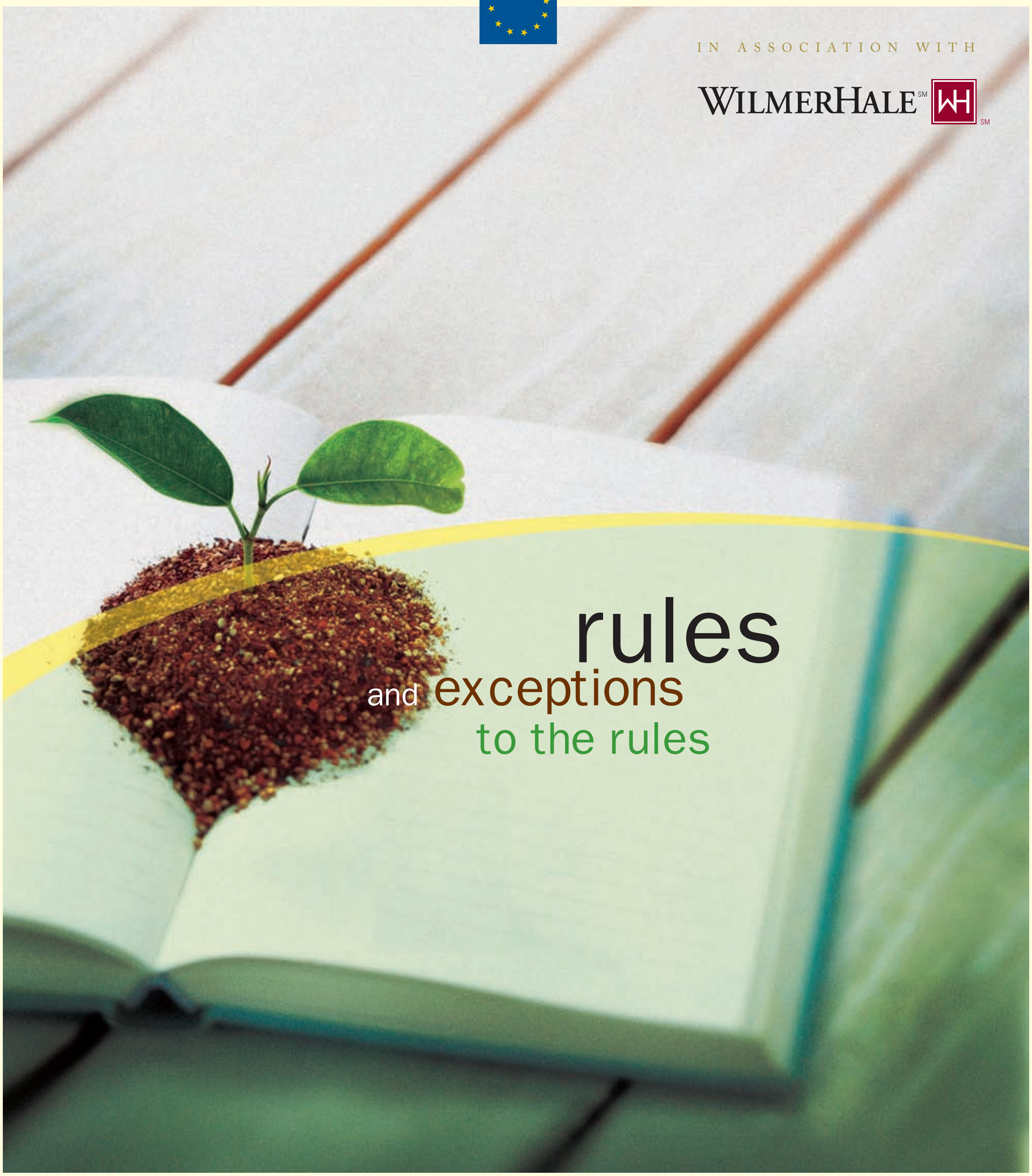
VentureEdge

EUROPE

2007 | €150



DOWJONES

don't like these odds? ...get VentureSource.

DOWJONES
VentureSource

+44 207 842 9858 | Sales@VentureSource.com | www.VentureSource.com

DOWJONES

Table of Contents

VentureEdge EUROPE

Floor 5, 12 Norwich Street, London, EC4A 1QN, UK
Tel: **+44 207 842 9898**

VentureEdge Europe 2007

Editorial: Stephen Harmston, Michelle Jeffers, Nicholas Smith

Research: Isaak Better, Victoria Camporeale, Jessica Canning, Arno Castanet, Gina Chan, Judy Chen, Steve Chen, Jonathan Cohen, Mickey Dai, Eva Ellehammer, Valerie Foo, Joshua Grove, Stephen Harmston-Green, Brendan Hughes, Shawn Jaswal, Antti Kantola, Angela Lee, Michael Little, Sabelle Mang, Benjamin Moscatello, Alexis Perry, Cameron Reece, Toivo Rehemets, Sarah Robinson, Anthony Sheldon, Nicholas Smith, Stephen Stuart, Daniel Wang

Design: Tuncel Gokcepinar, Tara M. Sapienza

Introduction

> *"The young man knows the rules,*
> *but the old man knows the exceptions."*
> — Oliver Wendell Holmes

'Less gets more' was the mantra for European venture capitalists in 2006. A total of €4.12 billion was invested in European venture-backed enterprises in 2006, the most since 2002, and median round sizes reached the highest level on record. However, these funds were invested across only 867 deals, the fewest annual total in at least seven years.

The main beneficiaries of this selectivity were companies seeking seed and first-round financings, which raised a total of €1.26 billion — a 31% increase from 2005 — and accounted for 40% of deal flow, the most since 2001. However, this renewed early-stage activity came at the marked expense of later-stage financings, which saw a 37% year-on-year decrease in deal flow and a 10% decrease in the total amount invested. In addition, the liquidity prospects for later-stage companies in the mergers and acquisitions (M&As) market remain less than ideal, with only 185 completed in 2006, down from 211 in 2005, and an average timeframe of 5.9 years from initial equity financing to acquisition, 12 months longer than in 2005.

Given these problems, the public markets represent an alternative funding opportunity for later-stage companies. Ninety-one initial public offerings (IPOs) were completed in 2006, coming on top of the 69 completed in 2005, which far outpaces the preceding four years. In fact, the robust climate for venture-backed IPOs in Europe, particularly on entrepreneurially-focused exchanges like AIM and the Deutsche Boerse Open Market, continues to surpass liquidity in the U.S. However, the relatively small amounts raised at floatation by European companies support the view that an IPO is increasingly functioning as a venture financing substitute for later-stage companies unable to access capital from traditional VC or private equity sources or to complete successful M&A transactions.

In common with later-stage financings, European venture capital fundraising activity slowed significantly in 2006. Coming off its highest level in three years in 2005, the €2.53 billion raised in purely venture capital funds in 2006 was down by 32% from the previous year, with a corresponding decline in buyout and other private equity funds.

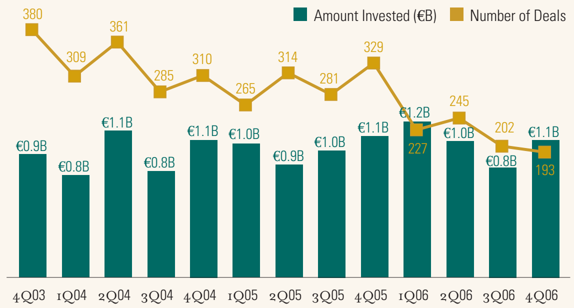
In summary, whilst 2005 was a year of rebuilding in the European venture capital industry, with total investment and deal flow besting 2004 levels, assessments of the success of 2006 will vary. Early-stage companies are receiving the level of financing they need to grow and compete in an increasingly global market, but at the expense of companies in later stages of development. Optimism about this revived early-stage activity, coupled with overall investment capital levels and public market liquidity opportunities, must be tempered by the notable slowdown in later-stage activity, global deal flow, M&A opportunities and fundraising.

Stephen Harmston | *Director, Global Research*
Dow Jones VentureOne

European Market Overview

2006

Figure 1: Deals and Amount Invested in European Venture-Backed Companies



Source: Dow Jones VentureOne/Ernst & Young | Underlying data available in **VentureSource**

Liquidity proved to be a key factor in the European venture capital market in 2006. The year ended with some 91 venture-backed, entrepreneurial companies completing initial public offerings (IPOs), the most IPO activity since 2000 for European-headquartered companies and surpassing the number of IPOs in the U.S. in 2006. However, much of this robust activity was aimed at furthering capital financing for what are still entrepreneurially-sized, endeavors – the total aggregate amount these 91 IPOs raised was only €1.75 billion, some 19% less than that raised by the 69 venture-backed IPOs completed in 2005.

Along with the improved liquidity climate, venture capitalists invested a total of €4.12 billion in 2006, the most annual capital investment since 2002. However, despite the larger sums invested, deal flow remains down with only 867 completed deals, the fewest since pre-1999. Investors appeared to be focused on financing selected companies with larger deals, although it remains to be seen if this newly constricted pipeline of entrepreneurial companies will result in enough successful exits to restore confidence in the European venture capital cycle.

After raising relatively large sums in 2005, European venture capital firms pulled back on fundraising in 2006. Only €2.53 billion was raised in purely venture capital funds, about 32% less than in 2005. The level of fundraising for buyout and other private equity firms in Europe also slowed from a year ago. The explanation may be that limited partners are

Figure 2: Largest Venture Capital Deals in Europe 2006

Company Name	Country	Close Date	Raised (€M)	Company Description
Plastic Logic	United Kingdom	31-Dec-06	€83.19	Developer of plastic electronics technology.
Icera	United Kingdom	15-Mar-06	€49.91	Provider of baseband integrated circuits for mobile devices and datacards.
Cerenis Therapeutics	France	13-Nov-06	€44.51	Developer of high-density lipoprotein related drugs.
Chroma Therapeutics	United Kingdom	31-Mar-06	€44.05	Developer of anti-cancer drugs based on enzymes involved in the remodeling of chromatin.
Nabriva Therapeutics	Austria	31-Jan-06	€42.00	Developer of small molecule antibiotics.
Ablynx	Belgium	23-Aug-06	€40.00	Developer of therapeutic nanobodies.
NovImmune	Switzerland	31-Oct-06	€37.46	Developer of immunotherapeutics.
Healthcare Brands International	United Kingdom	6-Oct-06	€36.71	Provider of over-the-counter pharmaceutical commercialization services.
U3 Pharma	Germany	22-May-06	€27.00	Developer of targeted therapeutic products for cellular signal transduction systems.
Novagali Pharma	France	31-Mar-06	€26.00	Provider of therapeutics for the treatment of ocular diseases.

pursuing interests in other areas of the private markets, and the tightened deal flow activity in Europe is constraining new venture capital fundraising efforts.

Despite the declining number of deals, several significant trends were in evidence in 2006. Among them was an increased interest in early-stage rounds, which represented 40% of all completed VC deals in Europe in 2006. This compares to about 32% in 2005. In terms of capital, €1.26 billion was deployed to seed and first rounds in 2006, about 31% more than in 2005. In fact, it was the most capital directed to these early-stage companies since 2001.

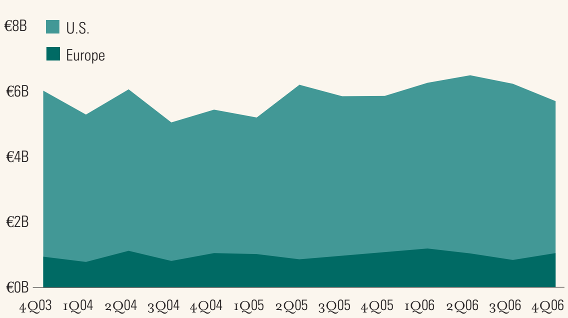
The median amount of capital invested in first rounds also increased, reaching €2.2 million from €1.5 million in 2005 and giving the highest median since 2000. Larger round medians were also apparent for second and later-stage rounds – the median amount invested in a second round of financing was €2.9 million, up from €1.8 million in 2005, whilst for later-round financings the median amount invested was €2.7 million, up from €2.3 million the year before.

The growing size of venture capital deals indicates that while fewer companies are able to secure a financing round, those that do are receiving larger investments with the potential to sustain them as they seek potential partnerships and/or exit opportunities.

Europe vis-à-vis the U.S.

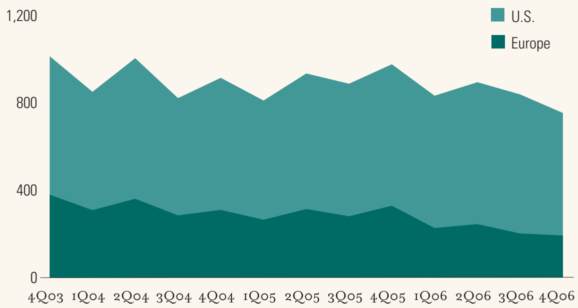
In contrast with Europe, U.S. venture capital activity increased in 2006, with a total of $25.75 billion invested across 2,454 deals. Deal count was up only 1% over

Figure 3: Investment Into Venture-Backed Companies, Europe vs. U.S. (€B)



Source: Dow Jones VentureOne/Ernst & Young | Underlying data available in **VentureSource**

Figure 4: Number of Venture Capital Deals, Europe vs. U.S.



Source: Dow Jones VentureOne/Ernst & Young | Underlying data available in **VentureSource**

2005, but the capital invested was up 8%. On a quarterly basis, deal flow and investment in the U.S. exceeded the levels of 2005 every quarter of the year.

For the second year in a row, U.S. investors focused more than a third of their activity on early-stage financings. Overall, seed- and first-round deals made up 36% of the deal flow in 2006 with around the same concentration of activity directed to later-stage deals. There was an overall balance of investment in 2006, with investors deploying significant amount of capital to later-stage portfolio companies but also supporting the emerging generation of new start-ups.

Later-stage rounds received $12.16 billion in capital in 2006, the most dollars directed to this round class since 2001, an example of investors continuing to support strongly the most promising portfolio companies toward an eventual exit. Second-round deals also received more capital, $6.13 billion, about 32% more than in 2005. Seed- and first-round deals captured $5.34 billion, 4% less capital but still relatively steady with 2005.

Interestingly, financings in the healthcare and business, consumer, & retail industries saw the largest percentage of early-stage deals in the U.S. In total, 39% of the deals to these two sectors were seed- and first-round deals in 2006 – indicating a significant level of interest in new start-ups in these categories. In comparison, only 32% of the year's information technology (IT) deals were early-stage financings.

Second-round deals in the U.S. represented only a small portion of the total financings – about 22% in 2006. This is slightly higher than the 20% of deal flow represented by these rounds in 2005, and may be a result of fewer completed early-stage deals over the last few years, leading to a dearth of companies in line for second-round financings.

The year saw improvement in the liquidity options for U.S. venture-backed companies. In total, 56 U.S. companies completed IPOs, up from 42 in 2005. However, these totals remain far off the pace of the previous decade. In the past few years, mergers and acquisitions (M&As) have played a much greater role in venture-backed exits, and continued to do so in 2006. A total of 404 venture-backed U.S. companies were acquired in 2006, consistent with the 407 acquired in 2005.

Within the U.S. venture capital market, IT still accounts for the majority of financings, with $13.76 billion invested across 1,446 rounds in 2006, representing 59% of the total deal flow. This is a slightly smaller proportion than in 2005, when IT deals made up 61% of overall deal flow, although total capital investment in IT surpassed 2005 by 2%. Within the IT category, deal flow for the information services and electronics and computer subsectors increased over 2005.

U.S. healthcare companies also showed increased investment levels over 2005. By the end of the year, 628 healthcare financings had raised a total of $8.25 billion, 31 more deals than the previous year and 12% more capital. Within the category, investment and deal flow in biopharmaceuticals – the largest segment – drove much of the growth in 2006, whilst investment in medical devices was also strong. Overall, healthcare financings made up about 26% of the year's total deal flow, up a single percentage point from 2005.

A renewed focus for the U.S. venture capital market is business, consumer & retail companies, which received $2.63 billion across 274 financing rounds in 2006. This represents seven more deals completed than in 2005 and 12% more capital.

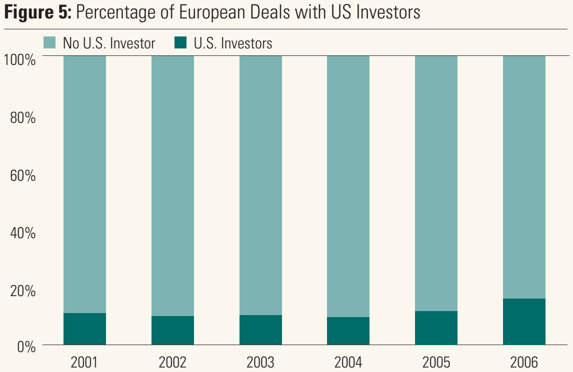
With 35% of the deals but only 20% of the money, European entrepreneurial companies continue to receive, on average, much smaller investments than their U.S. counterparts. This is a function of the relative size of venture capital funds in the two markets. The greater maturity of the U.S. market, and its larger returns to limited partners, has led to wider acceptance amongst investors such as pension funds and foundations. This has driven up the median venture capital fund size, which in turn has pushed up the average deal size. Other aspects being equal, this puts European entrepreneurs at a disadvantage.

With regard to the number of transactions, Europe hit an historical peak in 2001, when deal volume was about 82% of that in the U.S. By 2006, European companies were completing only 35% as many rounds as their U.S. counterparts. This remains low compared to historical levels, indicating that there is more room for short-term growth in the European market in terms of number of deals completed.

Individual Country Perspectives

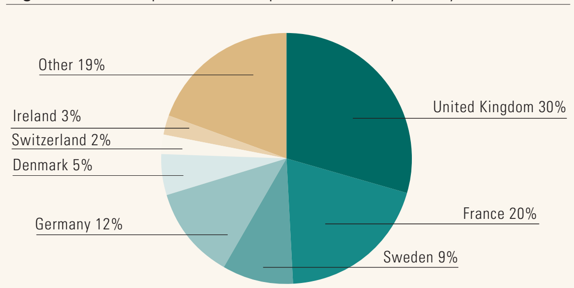
After a significant drop-off between 2002 and 2003, venture capital investment into European companies has continued to creep upward over the past three years. However, this is evident only in the amount invested, as

Figure 5: Percentage of European Deals with US Investors



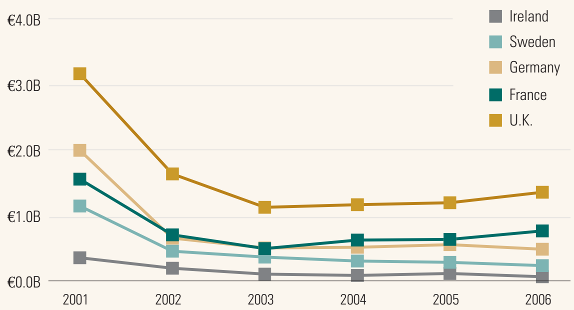
Source: Dow Jones VentureOne/Ernst & Young | Underlying data available in **VentureSource**

Figure 6: 2006 European Venture Capital Deal Flow by Country



Source: Dow Jones VentureOne/Ernst & Young | Underlying data available in **VentureSource**

Figure 7: Equity Investment in Europe for Major Countries (€B)



Source: Dow Jones VentureOne/Ernst & Young | Underlying data available in **VentureSource**

actual deal flow has continued to decline. Many European venture firms have been discussing the need to invest more money in fewer companies in order to compete with their counterparts in the U.S. Historically the average round size has been much lower in Europe, which has constrained the growth rate of European firms. However in 2006, the median round size was at its highest level and on a par with 2000.

Figure 8: 2006 European Investment Geographic Analysis

Region	Country	No. of Deals	Amt. (€M)
EASTERN EUROPE	Czech Republic	1	€1.0
	Estonia	2	€1.3
	Poland	7	€7.3
	Romania	1	€8.3
	Russia	1	€1.7
	Slovenia	1	€2.5
	Ukraine	2	€1.4
Eastern Europe Total		**15**	**€23.6**
NORTHERN EUROPE	Denmark	46	€228.7
	Finland	29	€110.9
	Iceland	3	€7.1
	Norway	19	€85.6
	Sweden	79	€249.4
Northern Europe Total		**176**	**€681.6**
WESTERN EUROPE	Austria	17	€120.9
	Belgium	26	€186.9
	France	171	€778.5
	Germany	105	€496.9
	Ireland	22	€79.0
	Italy	6	€25.8
	Luxembourg	1	€2.3
	Netherlands	17	€82.2
	Portugal	3	€5.5
	Spain	31	€116.5
	Switzerland	21	€149.0
	United Kingdom	256	€1,372.8
Western Europe Total		**676**	**€3,416.3**

The United Kingdom, which often bucks the trend of the rest of Europe, was in fact complicit in the deal flow declines in 2006. Venture capital activity in the U.K. faltered, with just 256 deals completed, down 31% from last year. However, the total amount invested in the U.K., €1.37 billion, was up 13% over the preceding year.

U.K. investors were focusing investments in 2006 on select companies with the highest potential. This seems particularly true in the IT category, where there were 31% fewer deals than in 2005 but 25% more capital investment. There is also a marked trend for early-stage investment in the U.K., which represented 52% of the deal flow, up from 41% in 2005.

The U.K. was responsible for some of the year's largest deals, including the fourth quarter's €83.2 million later-stage investment in semiconductor company Plastic Logic (Cambridge). Investors included Amadeus Capital Partners, Bank of America, BASF Venture Capital, Intel Capital, Merifin Capital, PolyTechnos Venture-Partners, and Quest For Growth, with Oak Investment Partners and Tudor Ventures as lead investors.

France remained the second most active European country for venture capital and investment grew here in 2006. The total amount invested, €778.5 million, was an increase of 20% from 2005. However, the total number of deals, 171, shrunk by 56, a year-on-year decline of 25%.

As for Europe as a whole, deal flow fell across almost all categories in France, with substantial declines for IT and business, consumer & retail companies. On a more positive note, French early-stage financings gained traction with 45% of the total deals in 2006 consisting of seed and first rounds, up from 36% in 2005. The largest deal of the year in France was a €44.5 million second-round investment in Cerenis Therapeutics (Labege), a developer of high-density lipoprotein-related drugs. Investors in the round included Alta Partners, EDF Ventures, HealthCap Venture Capital, NIF SMBC Ventures, OrbiMed Advisors, and Sofinnova Partners and was led by TVM Capital.

Germany, which saw steep declines between 2004 and 2005, continued to struggle overall in 2006. There were 105 deals and a total of €496.9 million invested, which is 24% fewer deals than in 2005 and 12% less capital. Information technology remained the dominant category in Germany, with 59 deals and a total of €269.4 million invested — this amount was in fact up 36% from 2005's IT investment totals. Early-stage activity also grew in popularity in Germany, representing 38% of the deals completed in 2006.

Germany was home to some particularly large deals: the €27 million investment in U3 Pharma (Martinsried), a developer of therapeutic products which target key components of cellular signal transduction systems, and the €23.3 million investment in CoreOptics (Nuremberg), a provider of high-speed transponder subsystems for optical networking equipment. Investors in U3 Pharma included Alta Partners, Atlas Venture, Bio M, Bio*One Capital, Edmond de Rothschild PE Management, and Life Sciences Partners BV. Investors in CoreOptics included Atila Ventures, Crescendo Ventures, GIMV, High Tech Private Equity, Quest For Growth, and TVM Capital.

Sweden was the fourth most active European country in terms of venture capital investment. However, both deal flow and investment declined in 2006, with a total of €249.4 million being directed to 79 financings, a 17% drop in capital and 29% fewer deals compared to the year before. Activity in Sweden was mostly focused on IT, which represented almost half the country's deal flow and capital. The information services segment was among the bright spots, with eight deals and €24.8 million invested in 2006, compared to three deals completed in the segment in 2005.

The U.K. still accounts for the biggest share of the market both in terms of amount invested (33%) and number of deals (29%). However, France has gained somewhat. Its proportion of the invested capital in Europe is 19%, up from 17% in 2005. The French percentage of total deal flow is steady at 20% in 2006, compared to 19% in 2005. Germany's representative percentage of activity has held steady for the past two years at 12% of all European deals. Germany also accounted for 12% of the total amount invested in 2006, down from 14% in 2005.

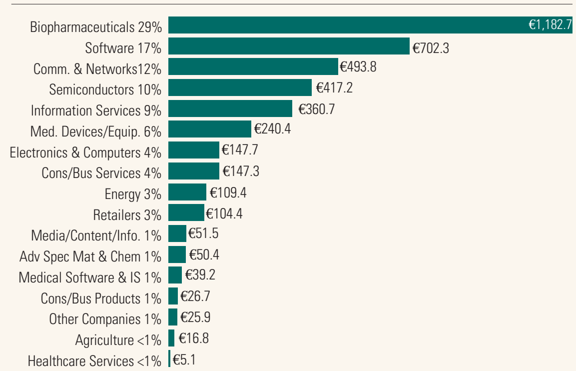
Major Venture-Backed Industries

Whilst deal flow declined among all major industries in Europe, investment into IT companies, bolstered by substantial capital directed towards those in the communications & networks, semiconductors and information services segments, held steady in 2006. There was a total of €2.12 billion invested across 472 IT deals this year, the most capital since 2002. The capital going to IT companies represented 51% of all the monies invested in 2006, compared to 46% in 2005. However, by refocusing on IT, investors turned away from healthcare. The €1.47 billion directed to healthcare companies in 2006 represented a 13% decline from 2005.

In terms of overall deal flow, IT continued to dominate venture capital activity in Europe. The 472 financing rounds represented 54% of the deals completed in 2006, about the same percentage as in 2005. Healthcare deals, which totalled 239, made up 28% of the overall financing activity, down from 29% the year before.

The business, consumer & retail category, which saw growth in 2005, continued to receive large investments in 2006. In total, there were 86 deals and €329.9 million invested here, 31% fewer deals than in 2005 but 26% more capital. As a percentage of total investment, this category represented only 10% of deal flow and 8% of capital investment.

Figure 9: 2006 European Investment by Industry (€M)

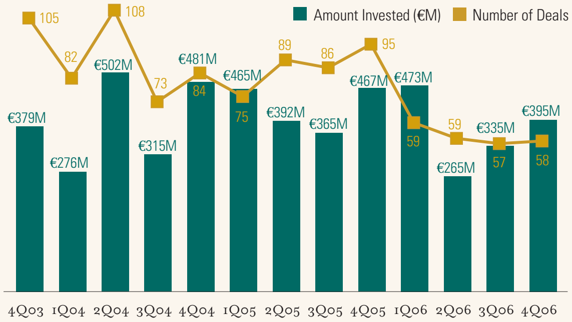


Source: Dow Jones VentureOne/Ernst & Young | Underlying data available in **VentureSource**

Healthcare Investment

Healthcare firms, unlike those in other sectors, have not witnessed as drastic a reduction in financial backing since 2000. One possible explanation is that venture

Figure 10: Venture Capital Investment in European Healthcare Companies



Source: Dow Jones VentureOne/Ernst & Young | Underlying data available in **VentureSource**

capitalists recognize that these companies require a longer investment cycle and are therefore financially prepared to support them for several years. If healthcare investment requires more patience and arguably more money, investors know that the potential gains are significant. The intrinsic lure of the sector also has been augmented by the steady flow of successful life sciences IPOs in the U.S. and Europe over the past two years.

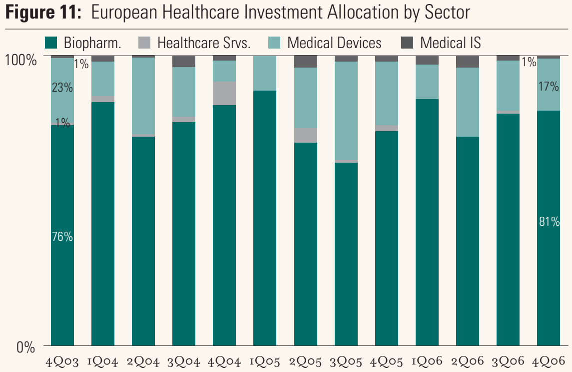
In the short term, the 31% decrease in financing rounds and 13% decrease in capital in 2006 was evenly distributed across most of the healthcare industry's segments. It was probably most noticeable in the biopharmaceuticals segment, where higher investments often bolster the outlook for the entire venture capital industry. Deal flow was down by about one-third for this segment and the capital invested was down 6%. Despite this, the segment was home to some of the largest European deals in 2006, including anti-cancer drug developer Chroma Therapeutics' (Abingdon, U.K.) €44.1 million later-stage round. Nomura International Private Equity Group and Wellcome Trust were investors in the round. There were also declines across the other healthcare segments. The only segment that held steady was the tiny medical software and information systems segment, which posted 15 deals and €39.2 million invested, four fewer deals that a year ago but consistent in capital invested. The median size of a healthcare deal in 2006 was €2.8 million, the highest on record.

Information Technology Investment

The IT sector led the way in venture capital investment in 2006. There was €2.12 billion invested in IT companies, 16% more than in 2005. Much of this capital boost came in the second quarter, which saw the most quarterly investment in the sector in four years. However, IT deal flow — at 472 financing rounds — was down by 185 deals from 2005.

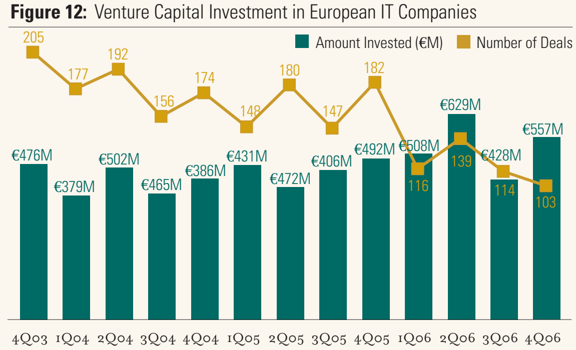
Within the IT industry, the Internet-heavy information services segment posted significant capital increases with 84 deals completed, three fewer than in 2005, but €360.7 million invested, up 32% from the preceding year. The segment was home to some particularly large online businesses in 2006. Larger deals for communications & networks drove total investment in the segment to €493.8 million, about twice as much as in 2005. More than €100 million more was invested in semiconductor financings in 2006, bringing the total to €417.2 million, although there were 23 fewer rounds. Software, the largest IT segment, posted 210 deals and saw a total of €702.3 million invested, down 13% in capital from 2005.

Figure 11: European Healthcare Investment Allocation by Sector



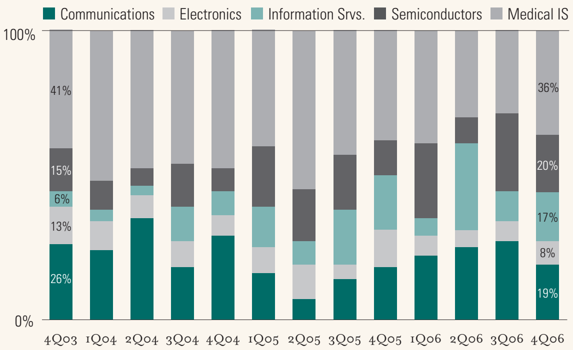
Source: Dow Jones VentureOne/Ernst & Young | Underlying data available in **VentureSource**

Figure 12: Venture Capital Investment in European IT Companies



Source: Dow Jones VentureOne/Ernst & Young | Underlying data available in **VentureSource**

Figure 13: European IT Investment Allocation by Sector



Source: Dow Jones VentureOne/Ernst & Young | Underlying data available in **VentureSource**

Business, Consumer & Retail Investment

Capital investment held steady in 2006 in the business, consumer & retail category, which saw a total amount of €329.9 million invested, 26% more than in 2005. Deal activity was, however, down with only 86 completed financing rounds, 38 fewer than occurred in 2005. Within the category, the consumer and business services segment, which includes many online businesses, saw a 12% jump in investment to reach €147.3 million. Media, content and information companies also benefited in 2006, with steady deal flow compared to 2005, and investment reaching €51.5 million, a four-fold increase. In addition, a particularly large investment in 2006 pushed the total amount invested in retail companies to €104.4 million, an increase of 47% from the year before.

The European market has seen increasing interest in emerging segments such as alternative energy and advanced materials and chemicals. A total of €109.4 million was invested into 27 energy companies in 2006, including Ocean Power Delivery (Edinburgh, U.K.), which received a €19.1 million second round deal in the second quarter. Investors in the round included 3i Group, Commons Capital, GE Capital Commercial Finance, Merrill Lynch Investment Managers, New Energies Invest, Norsk Hydro Technology Ventures, SAM Private Equity, Sigma Technology Group, and Tudor Ventures. In comparison, there were 20 energy deals in the whole of 2005, with total investment at €65.9 million.

Early Stage Activity

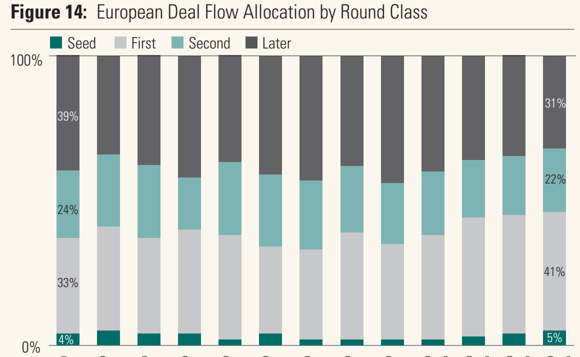
A positive signifier for the European venture capital market in 2006 was the renewed focus on early-stage investment, particularly in the fourth quarter when seed- and first-round deals represented 45% of all completed deals, the most since 2001. For the year as a whole, these financings represented 40% of the deal flow, up from 32% in 2005, thus creating a solid pipeline of entrepreneurial companies in the market. However, they still do not match the activity of 2000, when 62% of the deals completed were seed- and first-round financings.

In terms of capital, the €1.26 billion invested in seed- and first-round deals in 2006 represented a 31% increase over 2005. This is about 30% of all capital invested in 2006, compared to 24% of all capital in the preceding year.

On the other side of the coin, the number of later-stage rounds declined to 284, a 37% decrease from 2005, whilst the total capital invested in these rounds, €1.72 billion, was down 10%. As for allocation, later-stage rounds were responsible for 33% of the deal flow, compared to 38% in 2005. In terms of capital, these rounds represented 42% of all monies invested in 2006, compared to 49% of the total in the preceding year.

The switches between early- and later-stage investment form a natural part of the venture capital cycle. The success of venture capital in the U.S. in the 1980s was driven by the large flows of money invested in early-stage projects in the late 1970s and early 1980s. Similarly, the early 1990s saw a concentration on later-

Figure 14: European Deal Flow Allocation by Round Class



Source: Dow Jones VentureOne/Ernst & Young | Underlying data available in **VentureSource**

stage deals as investors picked up on the large flow of previous early-stage investments. This phenomenon has both positive and negative consequences. In some respects, venture capitalists have had little choice in recent years but to concentrate on later rounds. The significant spike in investment in the late 1990s and 2000 spawned a huge number of venture-backed companies, and combined with the contraction of the IPO and M&A markets, this meant that venture capitalists faced stark choices in supporting their existing portfolio companies. Each portfolio must have some successes – otherwise the firm will not generate the returns necessary to convince limited partners to re-invest. Venture capitalists were therefore conserving cash to support their existing portfolio companies through to successful exits. Investors must also factor in returns. Investing at earlier stages may yield potentially higher returns, but investing later can result in a shorter turnaround for returns – both of which impact IRRs. However, as the exit markets begin to improve, venture firms are cautiously redeploying capital to finance the next wave of start-ups.

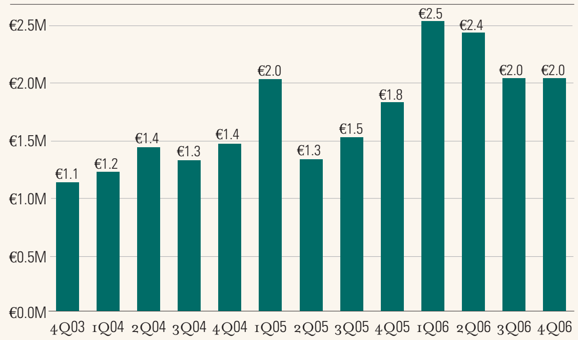
A year earlier, most investors considered the risk/reward trade-off to be more compelling at later stages. Companies that had already raised multiple funding rounds were more likely to have well-developed technologies or be approaching profitability (although this is more likely in IT than in healthcare). The risk attached to investing in these companies was much lower than for seed or start-up companies. At the same time, valuations were increasing for later-stage deals, reducing the long-term potential gains. But 2006 saw the pendulum swing toward investment at earlier stages in a company's development, where there is less competition between investors. Some investors also argue that company formations allow them to start with a "clean sheet", without the historical baggage of the restrictive terms often applied to prior rounds in a down market.

Capital Efficiency

There has been a strong negative correlation between the number of deals completed over time and the median time between financing rounds. Over the past several years, the median time between rounds has been creeping up quarter by quarter. In 2000 and 2001, the average period between financing rounds was less than 10 months, whilst by 2004 the average had reached nearly 20 months. For the last two years, it has steadied and by the end of 2006, it was closer to 18 months between rounds.

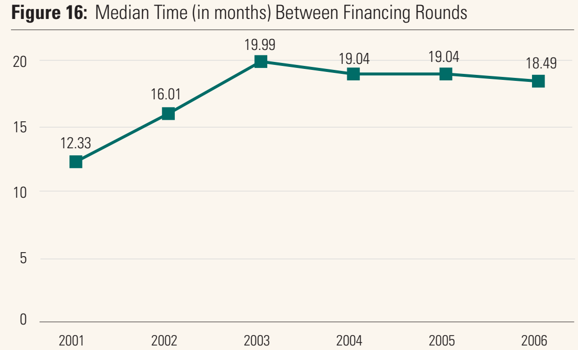
The increase in the median time between rounds since 2000 can be viewed as an adjustment to new market realities. In 2000, the business model for many venture-backed entrepreneurs involved swift expansion in a capital-intensive manner through aggressive advertising, infrastructure construction and product development. The short time between rounds in 2000 was a function of companies' high burn-rate, which in hindsight often seems to have been an inefficient use of venture money. In the current environment, the emphasis is on working venture money as

Figure 15: Median Amount Invested in European Financing Rounds (€M)



Source: Dow Jones VentureOne/Ernst & Young | Underlying data available in **VentureSource**

Figure 16: Median Time (in months) Between Financing Rounds



Source: Dow Jones VentureOne | Underlying data available in **VentureSource**

hard as possible, with ambitious plans for aggressive growth often curtailed in favor of cutting costs and increasing sales.

As the median time between rounds has increased, so has the efficiency of venture money. To attract funding, management teams have had to develop convincing business plans with measurable milestones, although this has led to increased time spent in securing funding at the cost of running their businesses.

Across Europe in 2006, the median amount raised by an entrepreneurial company increased to €2.2 million, the highest on record. For exclusively venture capital rounds, the median was slightly higher at €2.3 million. Much of this increase was related to larger investments in first-round deals, which also posted a median of €2.2 million, the highest amount for first rounds since 2000. The median size, €2.7 million, of later-stage deals represented the highest annual median for this round class since 2001.

Median deal sizes tend to be higher in the U.K. than the rest of Europe, and in both cases they tend to be much lower than in the U.S. However, the median round sizes were fairly consistent among the three major countries in Europe in 2006: the median in the U.K. was €2.3 million, compared to €2.4 million in France and €3 million in Germany.

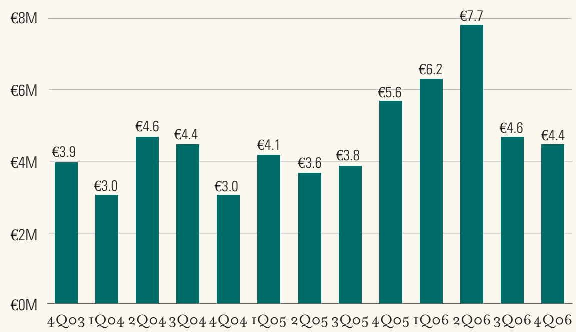
Valuations

Valuations are the result of different and potentially conflicting forces: the fundraising environment and the consequent level of capital available for investment; the exit market whereby successful M&As and IPOs help entrepreneurs running similar companies to strike better deals with their investors; the number of companies with a convincing business model; and the type of deals (i.e. seed vs. later, typically with a higher valuation).

In 2006, the overall contraction in venture capital investment and the positive liquidity environment led valuations to creep higher than 2005 levels. The overall median pre-money valuation was €5.6 million, the highest since 2000.

Accordingly, the median pre-money valuation rose

Figure 17: Median Pre-Money Valuation of European Financing Rounds (€M)



Source: Dow Jones VentureOne | Underlying data available in **VentureSource**

in the IT category, reaching €5.7 million in 2006, up from €3.8 million in 2005. The median valuation also increased for other major industries. For healthcare, the median reached €8 million, up from €7 million in 2005, whilst for business, consumer & retail, the median reached €6.3 million, up from €4 million. By round class, the median seed-round valuation grew to €1.9 million, the highest level on record.

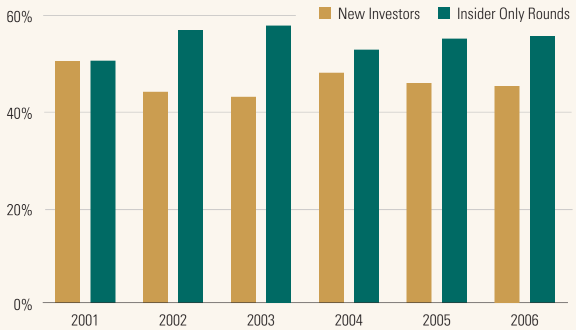
By country, the median valuation for companies based in the U.K. rose to €6.6 million, up from €3.7 million in 2005. The median valuation for companies in France increased to €5.3 million from €4.2 million. Germany's median valuations declined, standing at €4 million compared to €8.5 million the preceding year.

Investor Spotlight

In 2006, 3i Group maintained its position as the most active investor in Europe with 34 deals, of which 22 were investments in existing portfolio companies. The second most active investor was Sofinnova Partners with 24 deals, most of which (14) were follow-on financings in existing portfolio companies.

Like 3i, venture capitalists in general have, over recent quarters, been increasingly focused on existing portfolio companies and less on new investments. The percentage of overall initial investments has dropped from about 75% of the deal flow in the first quarter of 2000 to about 30% of investments in the first quarter of 2005. However, in 2006, that percentage has started to move upward and reached about

Figure 18: Follow-on Financing: Insider vs. New Investor Rounds



Source: Dow Jones VentureOne/Ernst & Young | Underlying data available in **VentureSource**

48% by the final quarter of 2006. The proportion of follow-on financing rounds which included a new investor also remained relatively low in 2006. In 2000, about two-thirds of follow-on rounds included new investors, while for the past three years the percentage of these rounds including new investors has hovered around 45%.

Fundraising

After a record-breaking 2005 for private equity and venture capital funds in Europe, the pace slowed in 2006. Firms closed on €27.15 billion in new funds, with the majority, €17.63 billion, committed to buyout funds. Venture capital firms raised €2.53 billion in the course of the year, down by 32% from 2005. The median size of a venture fund rose to €36.7 million, up from €30 million in 2005 and the highest median since 2002.

Unlike in the U.S., where nearly all the most active investors are pure-play venture firms, in Europe there is a broad mix of generalist private equity firms, investment banks and government investors, as well as corporate development and venture capital firms.

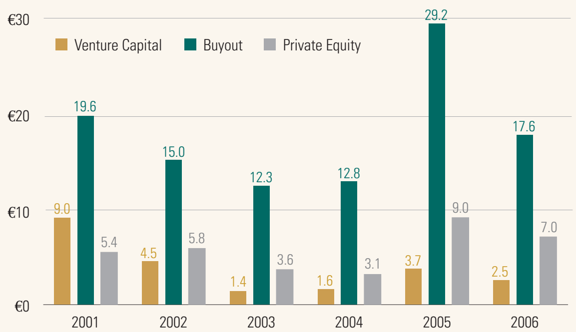
Figure 19: Top Investors in Europe 2006

Investing Firm Name	Initial Company Investments	Follow-on Investments	Total Number of Deals
3i Group	12	22	34
Sofinnova Partners	9	15	24
Seventure Partners	7	14	21
Index Ventures	11	8	19
YFM Group	14	3	17
CDC Entreprises Innovation	4	13	17
GIMV	9	7	16
Accel Partners	10	6	16
Vaekstfonden	3	12	15
Credit Agricole Private Equity	10	5	15
OTC Asset Management	12	2	14
InnovationsKapital	3	11	14
Enterprise Ventures Limited	9	5	14
SEB Foretagsinvest	2	11	13
Atlas Venture	8	5	13
Seed Capital Management	6	6	12
I-Source Gestion	3	9	12
Innovacom	2	10	12
TVM Capital	3	8	11
AGF Private Equity	9	2	11
Benchmark Capital	8	3	11
Scottish Enterprise	7	3	10
Quester Capital Management	5	5	10
Nordic Venture Partners	4	6	10
Life Sciences Partners BV	6	4	10
Amadeus Capital Partners	7	3	10
Industrifonden	3	7	10
Banexi Ventures Partners	5	5	10

Figure 20: Largest Funds Raised 2006

Investing Firm Name	Firm Type	Fund Name	Closed	Amount (€M)	Country
Cinven	Mezz/Buyout	Fourth Cinven Fund	3-Jan-06	6,500.00	United Kingdom
EQT Partners	Mezz/Buyout	EQT V	19-Dec-06	4,200.00	Sweden
Nordic Capital	Mezz/Buyout	Nordic Capital VI	24-Mar-06	1,900.00	Sweden
HgCapital	Other Private Equity	HgCapital 5	2-Mar-06	1,394.79	United Kingdom
Partners Group	Other Private Equity	Partners Group Secondary 2006	1-Oct-06	1,100.00	Switzerland
GSC Partners Europe	Mezz/Buyout	GSC European Mezzanine Fund II	12-Apr-06	1,000.00	United Kingdom
Palamon Capital Partners	Other Private Equity	Palamon European Equity II	28-Jun-06	670.00	United Kingdom
Gilde Investment Management	Other Private Equity	Gilde Buy Out Fund III	6-Sept-06	600.00	Netherlands
Phoenix Equity Partners	Mezz/Buyout	Phoenix Equity Partners 2006 Fund	14-Mar-06	550.58	United Kingdom
Ferd Private Equity	Other Private Equity	Ferd Private Equity Fund II	19-Oct-06	543.15	Norway
Gresham	Mezz/Buyout	Gresham IV	18-Jul-06	499.19	United Kingdom
Benchmark Europe	Venture Capital	Benchmark Europe III	15-Nov-06	457.55	United Kingdom
Deutsche Beteiligungs AG	Other Private Equity	DBAG Fund V	26-Jan-06	434.00	Germany
Waterland Private Equity Investments BV	Mezz/Buyout	Waterland Private Equity Fund III	10-May-06	403.80	Netherlands
Axcel Management	Mezz/Buyout	Axcel III	1-Apr-06	402.00	Denmark

Figure 21: European Funds Raised for VC, PE and Buyout (€B)



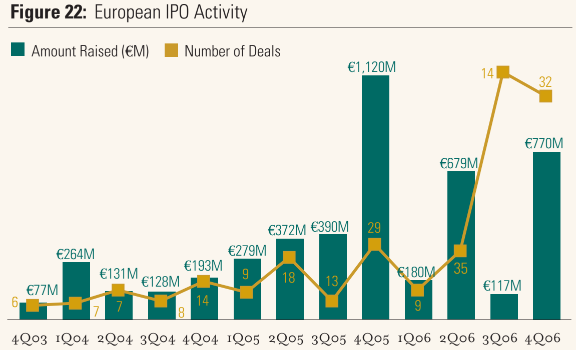
Source: Dow Jones VentureOne | Underlying data available in **VentureSource**

Liquidity

In 2006, 91 European venture-backed companies completed IPOs, surpassing the 69 which occurred in 2005. In fact, this is even more than in the U.S., which saw only 56 successful venture-backed IPOs in the same period. However, many European IPOs were smaller and can perhaps be considered additional venture financing rather than true exits from investors' portfolios. The total raised at IPO by European-headquartered companies was €1.75 billion, a 19% decrease from the aggregate amount raised by the IPOs in 2005. By category, the IPO companies were spread among IT (38), healthcare (30), emerging areas (12), and business, consumer & retail (11). The median pre-money valuation of the completed IPOs was €41.5 million, up from €36.7 million in 2005, whilst the median amount raised in equity prior to floatation was €7.1 million – down from €10.3 million the previous year. Companies still require an extended timeframe to go from initial equity financing to IPO: a median 5.9 years, about six months longer than in 2005.

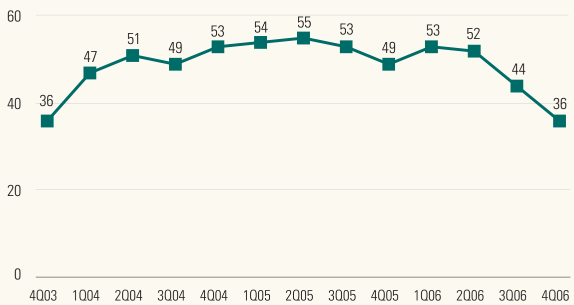
The ability of venture-capital supported companies in Europe to achieve IPO exits in larger numbers is clearly tied to the emergence of exchanges such as AIM, which provides a marketplace for relatively young entrepreneurial companies. The largest IPOs of 2006 were for companies that are not traditional venture-backed enterprises. Among them was the €99.67 million IPO for Vueling Airlines (BME: VLG), an airline service connecting Spain to other

Figure 22: European IPO Activity



Source: Dow Jones VentureOne | Underlying data available in **VentureSource**

Figure 23: European Venture-Backed M&A Transactions



Source: Dow Jones VentureOne | Underlying data available in **VentureSource**

European cities. It was valued at €348.9 million. The other was for Russian television networks company CTC Media (NASDAQ: CTCM), which raised €83.8 million in its June offering and was valued at €1.81 billion.

In other liquidity transactions, there were 185 M&A deals for European venture-backed companies in 2006, a decline from the 211 in 2005. The median amount paid for these companies was consistent with the prior year, standing at €18.7 million compared to €18.3 million in 2005. The median amount invested in these companies prior to acquisition was €5 million, the same median as in 2005. The companies took about 5.9 years from the time of initial equity financing to reach an acquisition, about a year longer than the median time to acquisition in 2005.

By industry segment, more than half of the 2006 M&A deals – 125 – were in the IT segment, while 33 were in the healthcare industry and 22 were business, consumer & retail companies. By geography, 49 of the acquired companies were based in the U.K., 28 in Germany, and 31 in France. The largest venture-backed M&A in 2006 was the €312 million acquisition of telecommunications networking software company Cramer Systems (Bath, U.K.) by Amdocs (NYSE: DOX).

Figure 24: Largest IPOs in Europe 2006

Company Name	Country	Industry Segment	Date	Post Value (€M)	Ticker Symbol	Exchange
CTC Media	Russia	Communications & Networks	1-Jun-06	1,891	CTCM	Nasdaq
Biovitrum	Sweden	Biopharmaceuticals	15-Sep-06	473	BVT	OMXS
Vueling Airlines	Spain	Cons/Bus Services	1-Dec-06	449	VLG	BME
Poliris	France	Media/Content/Info.	30-Dec-06	370	SLG	PAR
Parrot	France	Software	28-Jun-06	296	PARRO	PAR

Figure 25: Largest M&As in Europe 2006

Company Name	Country	Industry Segment	Close Date	Amount (€M)	Acquiring Company
Cramer Systems	United Kingdom	Software	15-Aug-06	312	Amdocs
KuDOS Pharmaceuticals	United Kingdom	Biopharmaceuticals	31-Jan-06	175	AstraZeneca
Chipcon	Norway	Semiconductors	24-Jan-06	166	Texas Instruments
NetCentrex	France	Communications & Networks	23-May-06	132	Comverse Technology

Interpreting the Global Rise in Private Equity Fundraising

Join us at the Private Equity Analyst Limited Partners Summit Europe | Now in its 4th Successful Year

The Private Equity Analyst Limited Partners Summit Europe returns to provide attendees with a comprehensive view of the state of the industry. Meet with industry leaders from around the globe, network with your peers and build relationships at our valuable roundtable sessions, and benefit from our editors' thorough coverage of emerging opportunities and risks.

PARTICIPATING FIRMS INCLUDE » 747 Capital - Access Capital Partners - Altius Associates - Bregal Investments - Capital Dynamics - Capitol Health - Grove Street Advisors - HarbourVest Partners - Hermes Pensions Management - Pantheon Ventures - Partners Group - Portfolio Advisors - Siguler Guff & Co. - Simpson Thacher & Bartlett LLP - Squadron Capital Advisors - Standard Life Investments VenCap International - TD Capital Private Equity Investors - Wellcome Trust - Wilshire Associates

REGISTER EARLY AND SAVE $300/€225

Call +44 (0) 203 2175 176 • Web: http://lpsummiteurope.dowjones.com/

Please use promotion code VEDGE

DOWJONES

Methodology

The findings in this report are based on aggregate data from VentureOne's proprietary European research. This data was collected by surveying over 1,200 active professional European investment firms, through in-depth interviews with over 7,000 company CEOs and CFOs, and from hundreds of secondary sources. The deals underlying this data can be viewed in VentureSource, the world's leading venture capital research database. • These venture capital statistics are for equity investments into early-stage, innovative companies and do not include companies receiving funding solely from corporate, individual, and/or government investors. • No statement herein is to be construed as a recommendation to buy or sell securities or to provide investment advice.

About VentureOne

Dow Jones VentureOne (www.ventureone.com and www.venturecapital.dowjones.com), a unit of Dow Jones Financial Information Services, has been the leading provider of finance and investment data to the venture capital industry for almost 20 years. Dow Jones VentureSource, a sophisticated electronic database on the venture capital industry, is published by VentureOne.

About Dow Jones Financial Information Services

Through its Financial Information Services group, Dow Jones produces focused, sector-specific online databases, newsletters and industry events for the private equity, venture capital and diversified markets. Newsletters published include Private Equity Analyst, VentureWire and Daily Bankruptcy Review. In addition, Dow Jones & Company (NYSE: DJ; www.dowjones.com <http://www.dowjones.com/>) is a leading provider of global business news and information services. Its Consumer Media Group publishes The Wall Street Journal, Barron's, MarketWatch and the Far Eastern Economic Review. Its Enterprise Media Group includes Dow Jones Newswires, Factiva, Dow Jones Licensing Services, Dow Jones Indexes and Dow Jones Financial Information Services. Its Local Media Group operates community-based information franchises. Dow Jones provides news content to CNBC and radio stations in the U.S.

IN ASSOCIATION WITH

WILMERHALE℠

About Wilmer Cutler Pickering Hale and Dorr LLP's Venture Capital Practice

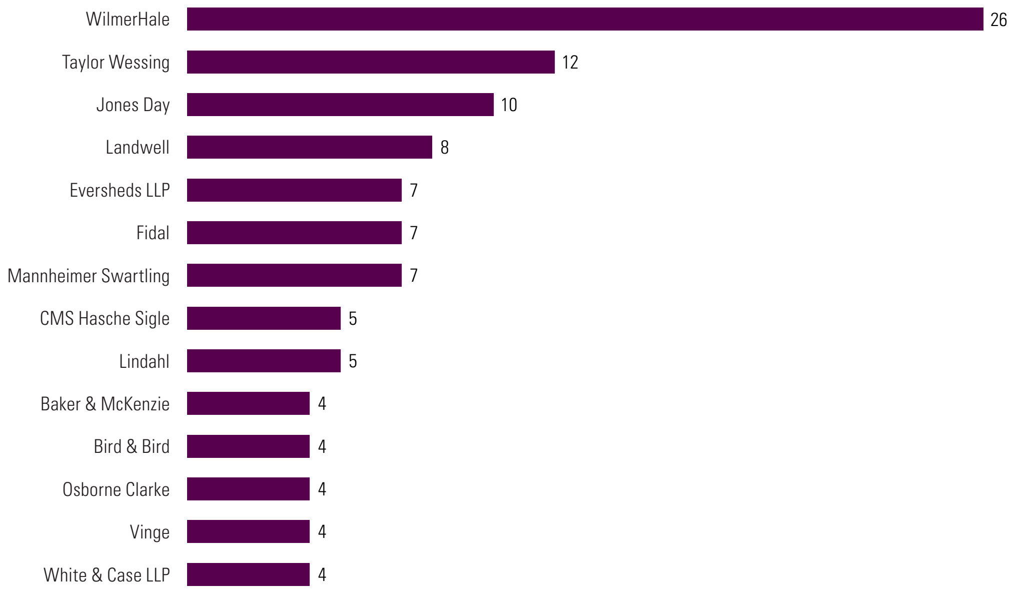
Venture capital transactions are a cornerstone of WilmerHale's corporate practice and reflect our long-standing focus on technology, life sciences and entrepreneurial companies. We have a strong presence in the venture capital community throughout Europe and the United States. We also represent leading venture capitalists in fund formation and portfolio investments.

In the past five years, we have served as company counsel in more than 750 venture financings raising over $10 billion. We represent more European venture-backed companies than any other law firm and we are counsel to more venture-backed companies based in the eastern half of the US than any other law firm.

We have more than 1,000 lawyers, and offices worldwide in Baltimore, Beijing, Berlin, Boston, Brussels, London, New York, Oxford, Palo Alto, Waltham and Washington. For more information, please visit our website at wilmerhale.com.

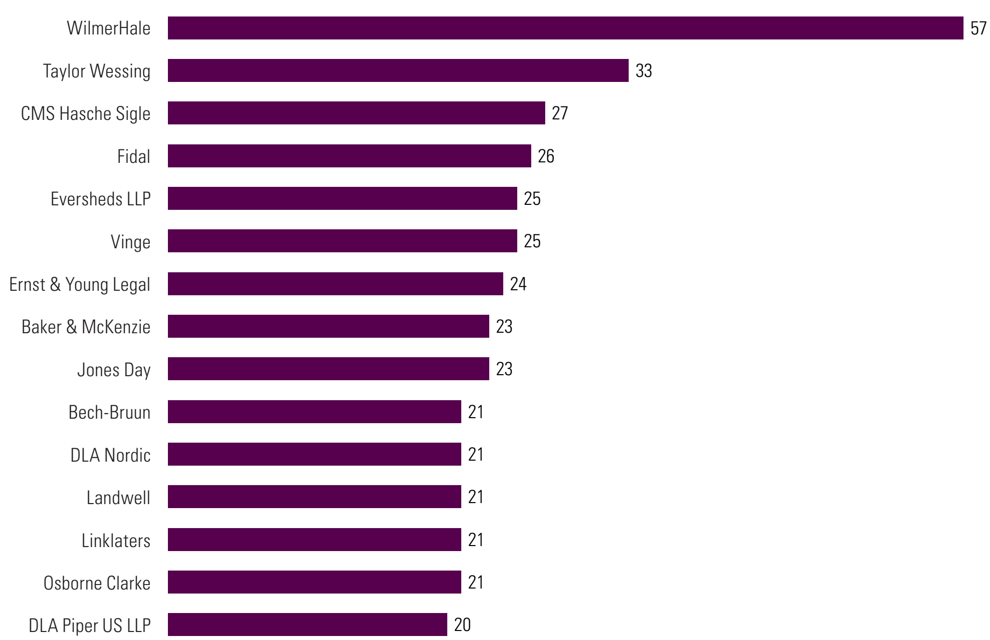
Law Firm Rankings – Europe

Counsel to Companies Receiving VC Financing in 2006 – Europe



The above chart is based on European companies that completed a seed, first, second, later-stage or restart round of venture capital financing in 2006.
Source: Dow Jones VentureOne

Counsel to VC-Backed Companies at Year-End 2006 – Europe



The above chart is based on European VC-backed companies that were private and independent as of the end of 2006.
Source: Dow Jones VentureOne