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Québec's Venture Capital Market in Q2 2011

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Québec's Venture Capital Market in Q2 2011 - Summary

Québec venture capital (VC) market activity showed growth in the second quarter of 2011, with \$112 million invested in total, up 11% from the \$101 million invested at the same time last year. Increased dollars also flowed to a greater number of Québec-based firms, which totaled 77 in this period, up 37% from Q2 2010.

Market outcomes for the first half of 2011 pointed to even more substantial expansion in Québec-based deal-making. Disbursement levels reached \$225 million at the end of June, or 23% more than the \$183 million invested the year before, while the number of VC-backed companies, totaling 130, rose 44%.

Québec VC trends proved somewhat more robust between April and June than elsewhere in the North American market. Across Canada, levels of activity actually registered a 2% decrease year over year, with \$328 million invested in total. In the same period, VC activity in the United States, totaling US\$7.8 billion, grew 9%.

As a result, Québec increased its share of the overall domestic VC market. Québec accounted for 34% of total dollars invested in Canada in the second quarter, which exceeds its historical market share, and for 57% of total companies financed.

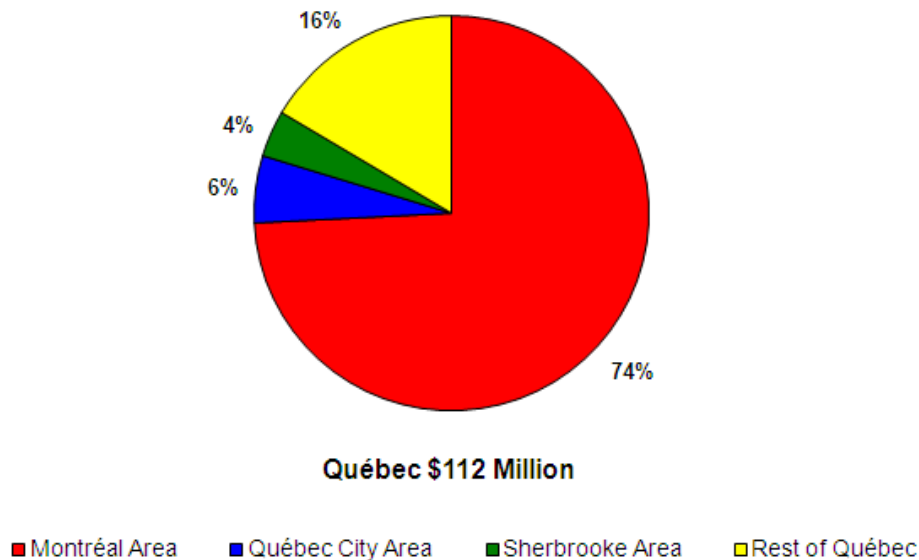
Growth was propelled in large part by activity in Québec clean technology sectors, which captured \$31 million in Q2 2011, up almost 10 times from the year before. IT-related and life sciences activity instead lost ground year over year, with \$23 million and \$19 million invested, respectively. Non-technology sectors were also a source of increased deal activity, with \$39 million invested this time around, up 58%.

Québec deal-making in the second quarter was led by locally-based VC funds and other Canadian investors, which put \$85 million to work. Labour-sponsored and other retail funds played a major role in this regard, investing \$59 million, up 41% from Q2 2010. Foreign investors also increased their presence in the Québec market, bringing \$27 million to deals, or nearly one-quarter of all disbursements.

Canadian VC fund-raising activity continued on a downward slope in Q2 2011, with new commitments totaling \$132 million, down 57% from the year before. Over the first half of the year, fund-raising fell 46%, though Québec-based VC funds netted 60%, or by far the largest share, of the \$374 million in cumulative new supply.

Given the greater growth in Québec firms receiving VC than dollars invested, deal sizes were relatively smaller in Q2 2011. Amounts invested per company averaged \$1.5 million, down from \$1.8 million averaged in Q2 2010. The period April-to-June nonetheless reflected closings of major deals, such as the financing of Montréal's Milestone Pharmaceuticals Inc.

Dollars Invested by Québec Region; Q2 2011



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After paying closer attention to new deals in the first quarter of the year, VC investors restored the focus to follow-on activity three months later. Forty existing portfolio companies captured 74% of dollars flows, or \$83 million, which is also up 13% from Q2 2010. Firms seeking VC for the first time also made year-over-year gains.

Montréal once again dominated Québec VC activity in Q2 2011, attracting close to three-quarters of all disbursements. Deal activity in other regions was led in Québec City, with a 6% market share, and Sherbrooke, with 4%.

Québec Clean-Tech, Traditional Deals Propel Growth

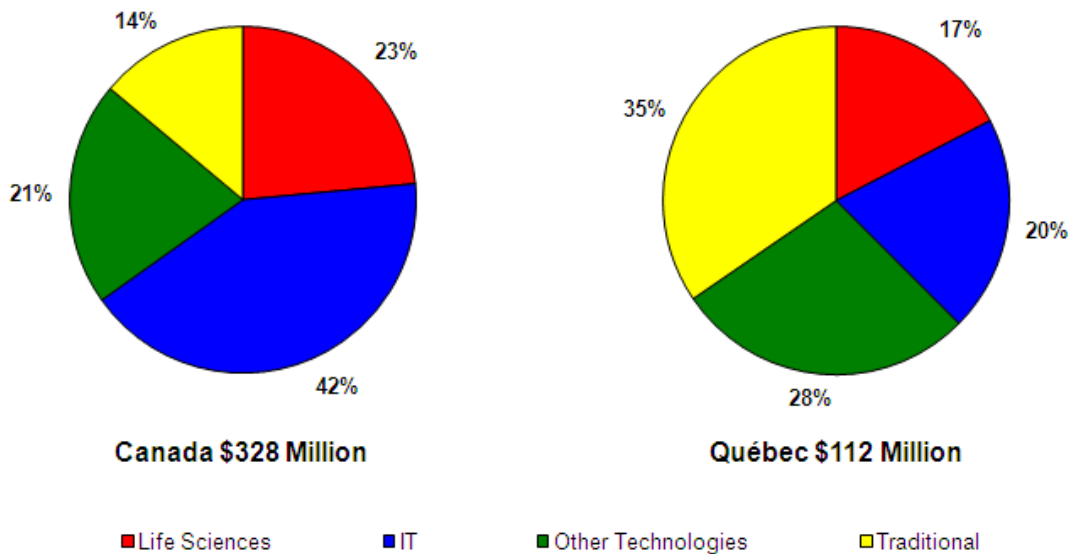
Among emerging technology sectors in Québec, information technology (IT) has most often been emphasized by VC investors in recent quarters. This was not the case in Q2 2011, however. This time around, overall growth in dollars invested was propelled in large measure by activity in clean technology sectors.

VC deal-making in alternative energy and other clean-tech sectors saw a total of \$31 million going to 5 companies in the second quarter, or almost 10 times the \$3 million invested the year before. Such activity, which included financings of the Montréal-based Enerkem Inc., and Terratube,

gave clean technology a 28% market share in this period, improving on its 11% share during the whole of 2010.

In contrast, Québec IT-related and life sciences activity lost ground year over year. Twenty IT companies absorbed \$23 million in Q2 2011, or one-fifth of the total invested, and down 27% from \$31 million invested in Q2 2010. This drop occurred despite substantially increased activity in specific sectors, such as electronics and hardware, which took \$13 million, in part due to a major deal involving Dorval’s Fleetmind Solutions Inc.

Dollars Invested by Sector; Q2 2011



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Levels of VC activity in life sciences sectors totaled \$19 million invested between April and June, reduced 52% from \$40 million invested at the same time last year. A dozen biopharmaceuticals firms accounted for this activity, which comprised 17% of all disbursements. In particular, Milestone Pharmaceuticals was the focus of the single largest disclosed VC financing in Québec in this period.

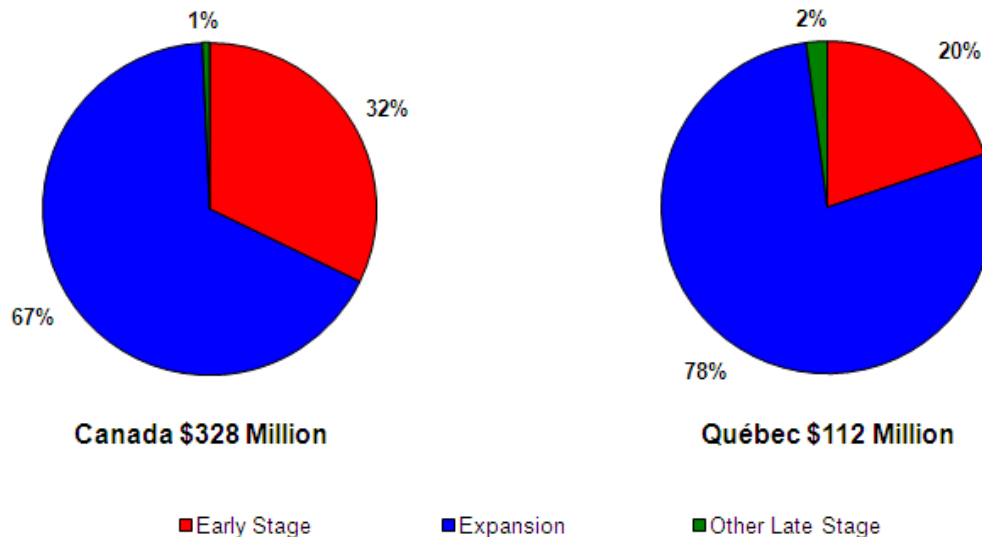
Non-technology sectors in Québec were also a source of increased deal activity in the second quarter. In total, \$39 million went to 44 companies, including Aviation Lemex Inc. of Saint-Hubert and La Forfaiterie Inc. of Stoneham, up 58% from \$24 million the year before. This gave traditional activity over one-third of total VC activity in Q2 2011, surpassing its 31% share during the entire of 2010.

IT-related activity continued to lead Canada-wide VC market trends in the second quarter, with \$136 million invested, or 42% of the total, though this reflected moderate decline from Q2 2010. Clean-tech activity instead experienced growth in this period, with \$66 million invested.

Québec Late-Stage Deals at the Fore

Companies at late stages of development were at the forefront of Québec deal activity in Q2 2011, consuming 80% of all disbursements. As in past quarters, the momentum was provided by activity in expanding firms, 54 of which saw \$88 million invested, signifying a 46% increase over the \$60 million invested at the same time in 2010.

Dollars Invested by Stage; Q2 2011



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In contrast, early-stage VC activity was eroded between April and June, with a total of \$22 million going to 19 companies, or 22% below the \$28 million of the year before. This overall result masked a modest uptick in seed-stage and startup activity, with \$1 million and \$3 million invested, respectively, in the second quarter.

Across Canada, expansion deals also made gains in Q2 2011, with \$220 million invested, or better than two-thirds of the total, and up 20% from Q2 2010. Early-stage VC activity instead decreased 24% year over year.

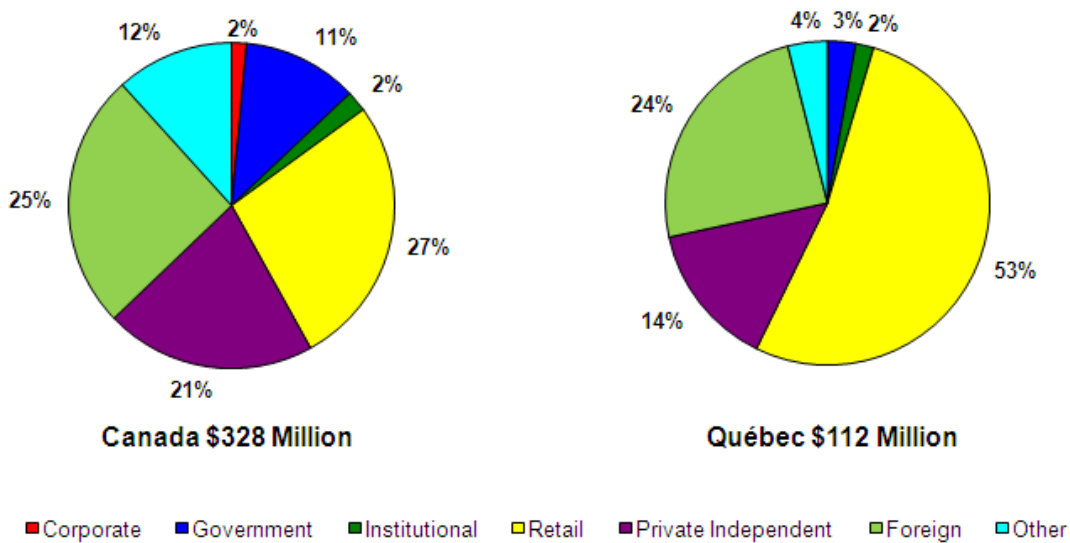
Québec Retail & Foreign VC Funds in the Driver's Seat

The bulk of Québec deal-making in the second quarter was assumed by locally-based VC funds and other Canadian investors. Taken together, domestic funds put a total of \$85 million to work in this period, representing over three-quarters of all disbursements, though activity was down slightly from \$88 million invested in Q2 2010.

Among locally-based VC funds, labour-sponsored and other retail funds played an especially important role in market trends this time around, investing \$59 million in 58 companies, which is up

41% from their \$42 million invested at the same time in 2010. Consequently, retail fund activity on its own accounted for over half of dollar flows in Québec in Q2 2011.¹

Dollars Invested by Investor Type; Q2 2011



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Private-independent VC funds also remained active in Québec between April and March, investing \$16 million in 17 companies. However, private fund activity was reduced 21% from the year before, when \$20 million was invested, and accounted for a somewhat smaller market share, relative to recent quarters.

Following a quiet Q1 2011, American VC funds and other foreign investors substantially increased their presence in the Québec market in the second quarter, bringing \$27 million to deals. Levels of foreign activity, responsible for nearly one-quarter of all dollar flows in this period, were more than double the \$13 million invested at the same time last year.

Foreign funds were also more of a presence in Canadian VC market activity in Q2 2011, bringing \$83 million to deals, or 25% of the total invested. Like Québec, domestic fund activity, totaling \$244 million, was down a fraction from the year before.

Canadian VC Fund-Raising Slows Further in Q2

¹ Québec labour-sponsored and other retail VC funds are increasingly doing a mix of direct investments and limited partner activity (i.e., making commitments to private funds). Both roles are relevant to reports of market trends, though data cited here reflect direct investments only.

In the second quarter of 2011, Canadian VC fund-raising activity continued on a downward slope. A total of \$132 million of new capital commitments was brought into the market in this period, or 57% below the \$308 million committed the year before.

Lower levels of fund-raising were also evidenced in the first half of 2011, during which time cumulative new supply reached \$374 million, down 46% from the same time last year. Funds headquartered in Québec netted 60%, or by far the largest share, of fresh VC resources obtained since the beginning of the year.

Retail VC funds led Canada-wide trends between April and June, raising \$97 million in total, though this reflects a 29% drop from Q2 2010, when these funds took in \$135 million. New commitments to partnerships fell even more sharply year over year, with only \$34 million captured this time around.