Portfolio Media, Inc. | 648 Broadway, Suite 200 | New York, NY 10012 | www.law360.com
Phone: +1 212 537 6331 | Fax: +1 212 537 6371 | customerservice@portfoliomedia.com

Medical Devices: What's Hot And What's Not

Law360, New York (December 03, 2009) -- Recent research regarding investments and mergers and acquisitions trends in the medical device industry suggests five overall trends in device industry transactions:

1) overall volume of exit transactions is down significantly during the first three quarters of 2009;

2) average deal valuations during this time are down by almost half, with increasing frequency of creditor- or investor-directed “date certain M&A events” (i.e., fire sales);

3) private equity buyouts comprise a much lower percentage of activity versus prior periods;

4) strategic acquisitions, while down in overall volume, constitute a significantly larger percentage of M&A deals; and

5) the volume of venture investment deals is down less than M&A, but the average venture deal size is down approximately 40 percent from last year.

The level of venture investment in the device industry during the previous decade was atypically high, and with ongoing structural changes in the venture capital industry, the lower volume seen this year represents a return to a more rational level.

Many observers believe that aggregate dollars invested in the sector are likely to remain at or near 2009 levels for the foreseeable future. Accordingly, companies will need to operate in a much less capital-intensive manner than times past.

Ability to self-fund (through family, friends and so forth) until the point of product validation is critical.

With venture capital funds much tighter and many alternative funding sources from past periods (such as direct investment by hedge funds) now effectively foreclosed, the following are areas believed to be the most promising funding sources for companies seeking “survival capital” in the current environment.

One key strategy is co-development arrangements, in which customers or prospective customers help fund product development and rollout in exchange for preferred access or other favorable terms post-development.

Where hospitals are customers, provision of access to facilities, personnel and infrastructure also can lower product development costs and stretch tight capital budgets.

Nondilutive funding sources such as philanthropic organizations, NIH funding/SBIR grants, and other grant programs at the state level also are increasingly seen as important sources of scarce capital.

It is important to note that philanthropic organizations have become much more rigorous in assessing potential grant recipients and that companies seeking such funding need to be prepared to make a strong, detailed demonstration of how they align with the target organization's philanthropic mission.

With increased competition for government funding at all levels, companies are well advised to obtain the appropriate professional guidance — strategic, lobbying and the like — to maximize chances for success.

Business models involving a long product-development cycle, from inception and product validation to the market, and requiring multiple infusions of large amounts of capital, are likely to continue to be out of favor for the foreseeable future.

Companies that survive and attract investment are likely to be those that can conserve capital, have the ability to get products to market with a small amount of investment dollars, and have well-thought-out and proven regulatory and reimbursement strategies.

--By Ronald S. Eppen, Foley & Lardner LLP

Ron Eppen is a partner with Foley & Lardner in the firm's Boston office.

The opinions expressed are those of the author and do not necessarily reflect the views of Portfolio Media, publisher of Law360.