MEDTECH INSIGHT
CITELINE COMMERCIAL

02 Oct 2023 | **Analysis**

'Build A Company To Be Bought, Not Sold,' 'Match The Asset To The Capital,' And Other Advice From VC Experts

by Reed Miller

At the recent LSX World Congress USA in Boston, *Medtech Insight*'s Reed Miller moderated a panel of experienced medtech investors to discuss the current medtech venture financing environment and offer advice for entrepreneurs raising money to support their innovations.

The medtech investment space has changed dramatically in the past few years.

The huge returns on investment that some investors were making in medtech prior to the pandemic have mostly disappeared. (Also see "*Investor Eye: Sofinnova Speaks On Deal Execution, Managing Expertise And what's In Store For The Future*" - Medtech Insight, 19 Dec, 2022.)

Inflation, the war in Ukraine, supply-chain disruptions, fears of a recession, and hospital-staffing shortages are all blamed for the decline in medical innovation investment. COVID-19 caused a spike in demand for remote and automated health care technologies. Connected care technologies are still attracting investment, but the enthusiasm for some of the digital health ideas that attracted huge investments just a few years ago has subsided, especially since brick-and-mortar hospitals and clinics reopened. (Also see "*Investor Eye: Sofinnova Partners Are Redefining And Disobeying The Venture Investment Commandments*" - Medtech Insight, 12 Jul, 2023.)

According to John Babitt from EY's life sciences group, new equity investment in medtech is at its lowest level in seven years. From July 2022 to June 2023, only $6.7bn of venture capital was raised by

Key Takeaways

medtech, Babitt reported at the recent LSX World Congress USA in Boston.

Merger and acquisition activity also continues to decline. Babitt pointed out that Johnson & Johnson's recent $16.6bn acquisition of Abiomed accounted for about 40% of medtech M&A activity in the last year. (Also see "J&J Pumps MedTech Growth; Offers $16.6BN+ For Abiomed" - Medtech Insight, 2 Nov, 2022.)

But, even as the investment market has changed in recent years, the fundamentals of what makes a company worth investing in have not changed. Success still requires preparation, integrity, determination, diligence, patience, foresight, and a sound strategy.

- Venture capital investment is down compared to just a few years ago, but there is no shortage of innovation looking for support.
- Companies can and should be creative about finding funding in this tougher environment, but some fundamentals about how to create relationships and build a strong business are just as true now as they always were.
- New companies should think just as carefully about their funding strategy as their technology strategy. And, of course, never be afraid to ask for advice from the investors trying to help them.

At the LSX meeting on 13 September, *Medtech Insight* editor Reed Miller moderated a panel discussion about how these attributes – among others – will help up-and-coming companies navigate the current medtech investment landscape.

The panel included five experienced medtech investment experts:

- David Kereiakes is a managing partner at Windham Ventures in Cincinnati, focused on digital health and medtech. He previously worked in Seattle for Providence Ventures, a strategic venture capital firm connected to Providence, a major not-for-profit health system across the western US. He has been a director for Bolder Surgical, TailorMed, MacroHealth, OrthAlign, DexCare, Wildflower Health, and AVIA Health.
- Daniel Gottlieb is an associate director at Broadview Ventures in Boston, which focuses exclusively on innovations to address cardiovascular disease and strokes. He previously led corporate development at Proteon Therapeutics and has also served in leadership roles in Abbott's endovascular business and Guidant's corporate venture arm. Gottlieb currently serves on the boards of XII Medical and Cardiosense and holds board observer roles at CroíValve and Nyra Medical.
- Hope Hopkins is the head of US accelerator programs for MassChallenge, a Boston-based,

non-profit "global network for innovators." MassChallenge has supported more than 4,000 startups in 24 countries with over $18m in equity-free cash. Hopkins previously worked in business development for the Rhode Island Commerce Corporation and as director of marketing communications for Ximedica, a medical-device development company in Providence. Hopkins also has about two decades of experience in consumer insights and strategic planning.

- Christine Hsieh is an operating partner with Third Culture Capital specializing in deep technology, data and strategic vision, and neurocognitive science. She is also an entrepreneur in residence at MIT's Martin Trust Center for Entrepreneurship, helping to forge industry-academic partnerships and advising entrepreneurs. Hsieh also serves on the board of directors for HealthTech Build, a Boston-based nonprofit that connects entrepreneurs, innovators, and physicians. She has a PhD in neurocognitive science from Harvard and MIT.

- Jonathan Gertler is the co-founder, managing partner and CEO of Back Bay Life Science Advisors in Boston as well as the managing director of Bioventure MedTech Funds. He is a former vascular surgeon and professor of surgery at Harvard Medical School. Companies he helped found include Antyllus Therapeutics, Optivio, and Cardiovascular Technologies. He also serves on the dean's advisory board at the Boston University School of Medicine and the Venture Advisory Board of the BioInnovation Institute in Copenhagen.

Here are a few highlights from the discussion, edited for clarity and length.

Q We hear a lot about how the VC environment has changed in recent years. What are the most important changes you have seen in this space?

A Kereiakes: [When I was at Providence at the start of 2022], we wanted to say, 'We're investing with diligence and with discipline.'

We're not chasing deals and we wanted to show our C-suite because we thought that it had become a bit exuberant. So, we looked at a bunch of deals where we had strategic support … and looked at the trailing 12 month multiple that was paid on those deals and for those 24 companies and found that the multiple of revenue was over 24 times. That is monstrous. That is huge.

Looking at it now, that has since been corrected, clearly, for better or worse. Companies are now raising funds at a more historical type multiple. Not in the 24x or 25x range. So at least that's what I've noticed has changed.

A Gottlieb: We don't usually look at an IPO as the expected path anyway, but one of the good things is that, from an acquirer perspective, at least in the cardiovascular [space], is that there are more [acquirers] out there.

You have *J&J getting back into the game in a big way with Abiomed* and building a franchise in that space again, and they're also selling their consumer units, so they are 'flush.' *You have Cordis … back in the game … with a really interesting business model*.

This second tier of companies – I only mean that from a size perspective – like *Shockwave* and *Inari*, and the others that are growing and need to fund growth opportunities if they're going to stay independent.

It seems like there are more players out there as potential acquisitions, which is great.

> *"People are being more creative … There is a lot more [interest] in research partnerships and other ways to get revenue early while you're trying to do your development." – Christine Hsieh*

A Hsieh: One key thing that I see that is changing now is that people are being more creative.

[They are] not just going to VC firms first – not a lot of money. There is a lot more [interest in] research partnerships and other ways to get revenue early while you're trying to do your development. And it's working. There's appetite for partnership, and you can actually get some of your development done in the meantime and try not to get waylaid on your strategy.

The best companies are still going to survive. But you have to be more creative in an environment like this. And hopefully that means better companies [will be] coming out for investment.

A Gertler: One thing that always bothered me about this as a clinician is that we have biopharma and we have medtech as two separate monoliths.

But there isn't a clinician in the world that divides his or her attention into drugs [versus] devices. It's all solutions for patients.

We are seeing, increasingly, in medtech and even in healthtech, that we're introducing physiology and biology impacts on a much more profound level into the application of medical devices. And that was previously [only] the domain of biotech.

That's an enormous change for us. And we're no longer wed to anatomic widgets and we're much more led by physiologic impact. And I think that's going to be the thing that carries this field forward for a long time to come.

Q What has not changed? What are the most important fundamental characteristics you look for in a company?

A Kereiakes: I never invest with the mindset or with the thesis that 'This [company will exit with] an IPO. Eleven out of 10 times, I'm selling through a 'strategic.' It just works out far better.

> So, the mantra I always live by is that you build a business to be bought, not sold. You build a good business. You always use that as your North Star –what makes us a great business and 'How do I continue to build it?'

"The fundamentals of what we look for in a company are the same…We look for good teams [that are] addressing unmet needs." – Daniel Gottlieb

---

A Gottlieb: What hasn't changed [is that] the fundamentals of what we look for in a company are the same.

We look for good teams [that are] addressing unmet needs, with a clear development path in something that's protectable. I don't think that's changed.

There's still money out there to invest. Valuations may be down, but those kinds of companies are still getting funded.

A Hopkins: We [at MassChallenge] don't invest, other than a lot of time and emotional energy, nor do we take equity.

So I would take the antithesis view of this and say that nothing has changed because the FDA hasn't changed and the companies that we want to support still need to hit [the same] 'litmus test' [that they always have]: A plausible pathway to [market] traction and actually becoming a company of revenue-positive impact on the world.

"Don't pay attention to the cycle. Have a long-standing strategic

---

view. That includes financing, but also company development." – Jonathan Gertler

A Gertler: I think we're facing [as always,] 'cycles.' I couldn't care less about cycles.

I'm sorry to say that those are things that you have to maneuver through, but we shouldn't pay attention to them. 25 years ago, around when I started in this business, there were cycles that were crushing ... [but] medtech is here to stay and biotech is here to stay.

Don't pay attention to the cycle. Have a long-standing strategic view. That includes financing, but also company development.

The other thing I don't care about is trends. If you've ever watched a third-grade soccer team, the ball goes in the corner and 11 Children run into the corner. Who cares? It's not the way to put the ball in the goal.

All you should care about is fundamentals, unmet need, clarity of vision, and execution, and then link the financing strategy to that.

Q **Are there a few common misunderstandings that you encounter repeatedly? Put another way, what are some of the challenges that new medtech entrepreneurs frequently do not understand or underestimate?**

A Gertler: There needs to be a real ... marriage of the technology – whatever technology you're working with – to the clear solution that you're going after and the ability to extend that solution.

And if you don't have a clear vision of the clinical indication, the need, the application and the path to get there, then it will be a very, very tough row to hoe.

When we sit down with them, if we don't hear that vision, then it's going to be hard to fund the company.

The other thing that is underemphasized is that financing is as strategic as is any other technology or clinical development pathway. And paying attention to the long run of your financing strategy is clearly something that has to happen. We all need to remind ourselves of that over and over again.

"A pet peeve of mine is when [I meet a] a technical founder and [they're] showing me a business on paper, but [they] haven't really done anything to actually validate that market yet." – Christine Hsieh

---

A Hsieh: A pet peeve of mine is when [I meet a] a technical founder and [they're] showing me a business on paper, but [they] haven't really done anything to actually validate that market yet.

Have you gone out and talked to 100 Doctors? Have you gone out and walked a mile in their shoes and figured out who is the actual end user?

And it happens so much because, a lot of times, the technology is spinning out of a lab … or academics who are passionate about a certain field, but [are working toward a] 20-year horizon in a research lab.

[But] does this have commercial potential? Is this the right time to commercialize this thing right now? That's going to depend on what's actually happening in the clinics and in the hospitals [or] maybe what's happening in reimbursement.

So [they need] a wider lens and they really need to have done homework.

A Hopkins: I looked up some of our data. In [MassChallenge's] cohort this year, which is comprised of 53 founders, 42% [already] have customers, but of that 42% only 63% have *paying* customers.

So therein lies 'conversation number one.'

Conversation number two: We always ask [potential partners] at the beginning of the program to state the different goals that they want to work towards, in the construct of either three or six months … [Our survey of their answers showed] they actually 'over-indexed' fundraising as their number one goal and then their secondary goal is networking.

And they 'under-indexed' – by -13.6% compared to other industry sectors – product market, fit, and business strategy.

"There's a lot of what should be fairly easy-to-do prep work so that you maximize your chance of having a good impression on the first meeting." – Daniel Gottlieb

A Gottlieb: There's a lot of easy work that can be done in advance. [That is] really low-hanging fruit and easy, but it's something I don't think entrepreneurs think enough about when they're meeting with investors – to come into the meeting prepared. [And they get] typically, one shot; a half an hour to an hour.

Just do background research on 'Who am I meeting with what's their backgrounds? Do I have a connection with them? Do they have an investment in this area already?'

[Maybe they] don't have to spend 10 or 15 minutes doing the background on the technology. [For example,] we've done [many] investments in cardiovascular disease, so we don't need to have the background on what heart failure is. But they might say, "Okay, got it ... Well, let me show you this one thing on slide one about heart failure and it goes on for 10 minutes."

And...bring people into the meeting that can answer the questions that may come up, [such as,] 'What are you looking for how much money you're trying to raise? What's the milestone that you're going to hit with that money? What's the value creation?'

There's a lot of what should be fairly easy-to-do prep work so that you maximize your chance of having a good impression on the first meeting. And all you want out of that first meeting is a second meeting.

A Kereiakes: The core of what we're all outlining is communication skills. A good communicator is a good listener and [they are] coachable in general.

My success has been alongside some incredible entrepreneurs. And those entrepreneurs, [can] communicate a complex concept which, in health care, is [a] value proposition that has to be tied to an outcome [that shows] why somebody should pay for it. And there are plenty of reasons why people don't pay for stuff in health care.

So being able to articulate [that value proposition], in a short period of time, to somebody like me [will make it possible to also] convince a very smart physician or an administrative leader – who doesn't have the budget or doesn't want to listen – [to] understand why they need to buy it.

A Gertler: As investors or even as advisors, at the end of the day, we have a job which is to be able to recognize value and return capital … but we also have assets to manage and returns to come up with.

[I agree with the previous points about] preparation, finding the outcomes, and beginning with the end in mind. [Also], make sure you're still building for sustainability, because you don't know what ‘cycles’ are going to do [to the market].

I’ve sat on all sides of these ‘fences.’ You’ve got to figure out how you can meet in the middle productively because, at the end of the day, we bet on management teams more than anything.

“Saying ‘I'm going to sell this business upon this milestone to these groups for this amount,’ just shows a lack of sophistication or just a lack of awareness.” – David Keriakes

Q If you ask an innovator or entrepreneur, ‘What future do you see for your company?’ What kind of answer do you hope to hear?

A Kereiakes: It's a broad question, directionally speaking, but again I’d say, ‘You build a business to be bought, not sold.

Saying ‘I'm going to sell this business upon this milestone to these groups for this amount,’ that just shows a lack of sophistication or just a lack of awareness.

The [potential] acquirers can sense that. And then there's nothing pushing them to buy [it.] Then you have to bluff.

And, in that preparation leading up to that point, you will start signaling [a bluff] if you don't, [for example] hire a sales leader, or if you don't raise the kind of capital that you need … or don't invest in R&D … or you don't have those [critical] conversations with the physicians who will be the end customer, or you don't start reimbursement discussion.

[Instead of thinking that] you're running a race and then say ‘there's a finish line,’ [you should be] always running well past that. It is always important for me to understand how you are building a good business here and where the is market moving.

[But] maybe you can steer the market and help lead the market. Do that and somebody will buy it.

Q **Are there any other major pitfalls or ‘landmines’ in this venture investment process that are often overlooked? Put another way, what is an important example of something that you know from experience that you wish you knew when you started in this field?**

A Gertler: Again, the greatest landmine [for a company looking for investment] is, ultimately, a lack of lack of preparation and understanding, [of] what you have.

I always use the term ‘control the debate.’ [If you are prepared], you may still have your own biases and you may have data sources that actually have not served you completely, but at least you will have a base of an argument. [Investors] will pick it apart and so you have to have ready answers and at least a plan that will allow you to create a productive argument [such that] you're not just back on your heels and having terms dictated to you.

[Also, all too frequently] people don't match their technology – their asset or their invention – to the right structure for building a company.

Match the asset to the capital.

MEDTECH INSIGHT
CITELINE COMMERCIAL

Medtech [has] three categories, broadly.

One is the far-reaching, absolutely 'crazy' idea. [For example, angioplasty], 35 or 40 years ago, was nuts. Who would blow up a balloon in an artery, especially one leading to the brain? That was crazy. But it turns out that it works, and now there is an incremental improvement every couple of years in balloon profiles. But at that time, it was more than radical. It had a ‘biotech profile,’ which means about 99% of those things fail and 1% really succeed.

The vast middle in medtech are those [ideas] which are really predicated on very sound engineering and clinical principles, but somehow are meaningfully improving them. In order to come to an investor with that kind of story, you have to really understand why it's meaningfully improved and how you can change behavior [to drive adoption.]

And then the third category [of technology] are the extremely valuable-but-incremental improvements. That really has no place in a venture fund.

There is nothing wrong with that. It's an extremely valuable contribution. It's just the wrong ... asset-to-capital match up. That's where the pitfalls are that people should pay more attention to.

> ***“Their number one pitfall is they're totally dishonest with themselves... In fact, they do not want to leverage their entire life savings, mortgage their home, and only eat ramen at 30-something years old.” – Hope Hopkins***

A Hopkins: [I would] emphasize the human in the middle of this...So, 'soft skills.'

A lot of the startups that I see are first-time founders. And there's a real martyrdom in this space because largely they get into it, or they start to solve the problem, because they've seen something in their family or it's through first-and experience.

And their number one pitfall is they're totally dishonest with themselves... In fact, they do *not* want to leverage their entire life savings, mortgage their home and only eat ramen at 30-something years old.

Know thyself.

You've got to give yourself some runway until things get real and you have a quality of life to maintain.

A Kereiakes: [As Christine said,] entrepreneurs are getting more creative.

You had, historically, a debt ‘credit card’ and an equity ‘credit card,’ [to fund a company]. Increasingly, there is also a third one. It's your customer or distributor or other ways to pre-fund a sale to ... pull cash from operations to help offset the lack of equity [available] out there.

Amazingly, that is still fairly available and it's fairly aggressive.

A big mistake that I see [comes from the problem] that this [kind of deal is] really hard to unwind.

Distribution agreements [with bigger companies] that a lot of startups [will] sign are a great way to generate revenue and it's a very efficient way to leverage the sales reps that a [big] medtech companies has.

Unfortunately, when you sign those agreements, there are a couple of different scenarios. [If you rely entirely on that distribution partner] and so you don't touch the physician or that end clinician or the purchaser, [that partner is] not going to just pay you for their revenue. They won't because the moment they do that, that turns off and you are stuck with zero. So, then you're held hostage at that point.

And if it does not sell well … then you're stuck.

[But if that partner has moderate success selling your product], hopefully you've still built enough of [your own] direct sales force and you can have some argument to say, ‘There's value here and we've proven that it can work.’ And yet you also still have enough revenue and 'touch points' into the customer that you can get an exit.

But I find those distribution agreements increasingly [common] now because funding is harder to come by.

A Gottlieb: Entrepreneurs [should] ask for and accept help. And often these entrepreneurs are people that are wildly successful in their fields, but this is a completely different ballgame for them.

There's asking for help and then there's also accepting help, and that's certainly where we get into a lot of trouble with those people who think they know the right way when we're trying to be helpful.

And giving up control is really hard for people when it's 'their baby.' But that's often, at some point, the right thing to do. … Ultimately the best way to get success is to bring in the right people, the right resources, and optimize across all of that.

A Hopkins: Our whole thesis is knowledge and networking connections.

At the earlier stages, we are immersing [innovators] in knowledge so they don't waste any of our time, frankly. Networking [means] getting that strategic exposure to companies that aren't necessarily going to become your future customer.

They may but it's that trial period of trying out a ‘use case,’ or connecting this person to that person, and [trying to] formulate your hypothesis further in a real in situ opportunity and then the connections are right then you're ready, when it is looking like your pitch is solid.

[VC investors have] flooded inboxes … seeing hundreds if not 'millions' of deals a year. So we want our start-ups to come in the best position to sound knowledgeable about their project. … And you really educate them on being more hard-hitting, direct, and thoughtful in how they present.

“What's your role going to be in it and how is this going to spin out? You have to figure that out first before you go along this path.” – Christine Shieh

A Hsieh: [The university innovators that I work with] have to decide if they're going to be the ones to be really strong commercially.

‘Are you the founder who was [also] the researcher [who is] also going to go and sell this now? [Or will you hire somebody else to do that]?’

When people are equivocating between those options, they may kind of get stuck. And so there's almost an identity crisis.

Even if you are [university] faculty, are you going to start this company with a postdoc? What's your role going to be in it and how is this going to spin out? You have to figure that out first before you go along this path.

Otherwise, your technology is just going to sit there.

And it is often not being communicated the right way. Academic talk is very different. And it's very hard to break out of, in many cases, 15 to 20 years of research talks. You can't explain *so* much of your technology. [You need to pitch it with] one or two slides [about] how it works and the 'killer difference.'

You need to be able to communicate in a way that shows the potential for growth – that kind of final vision.

Q Finally, I know you have all thought of at least a few things you would really like to change about venture capital in medtech. Can you share any of those ideas?

A Gertler: Empathy...Just as a broad categorical comment, I think it's entirely lacking in our society at the moment. It doesn't need to be empathy without discipline. [But] at the end of every day I return emails, even if it just says 'I'm terribly sorry, this [proposal] isn't a fit for us.'

It's 30 seconds at the end of my day. Incidentally, in self-interest, it spares me five more in emails and guilt. But, also, it's incredibly courteous.

For somebody to sit on top of a pool of capital ... and not showing respect to people who were putting themselves completely at risk, I think is wrong. We all fail at it. We can't do it all. But I don't think it's wrong to ask for empathy from the investor to an entrepreneur, delivered properly.

If you find that a investor is just not responding to you, despite your entreaties, and is really treating you rudely, that's probably not somebody that's going to be there for you in the trenches. Because, inevitably something is going to go wrong. And I think we just all need to remember this on both 'sides of the fence' and I don't think we remember it enough.

"It would be nice to just see more trust developed so that the advice that's given, even when you pass up on a deal, is taken to heart." – Hope Hopkins

A Hopkins: I live in the world where venture capital is commonly referred to as ‘vulture capital.’ So, [I would like to see a shift toward] a greater embodiment of trust between [investors and companies].

Because you're not trusted. You're [treated as] a necessary evil and as somebody that provides capital. [That is] until you invest in their company, and then you're 'absolutely a great partner in the effort.'

But just getting to that point, it would be nice to just see more trust developed so that the advice that's given, even when you pass up on a deal, is taken to heart versus pushed to the side because you're just on to the next and it's very transactional.