VENTURE PROFILE

USVP Aims Early, Finds Success Later

Firm Has Benefited From Push Toward Less-invasive Procedures

By Brian Gormley

Though **U.S. Venture Partners** devotes only about a quarter of its capital to health care, it has succeeded by getting ahead of several key trends.

The Menlo Park firm was an early proponent of the drive to replace surgical treatments with catheter-based ones, for example, backing companies such as Advanced Cardiovascular Systems, a maker of balloon-angioplasty catheters now part of Guidant. It also was an early backer of biotech companies Amgen and Xoma.

Today, the firm, which will soon begin investing its new, $600 million fund, is striving to take a lead in emerging fields such as congestive heart failure, spinal disorders and drug-device combinations.

USVP, whose health care team is led by General Partners Philip M. Young and Dr. Jonathan D. Root and Partner Alan L. Kaganov, also has been one of health care's more consistent investors. Since forming in 1981 the firm has allocated 20 percent to 30 percent of its funds to health care, even as other technology-oriented firms abandoned it. The partners also resisted the trend in recent years toward late-stage investing, keeping to their traditional practice of investing relatively small amounts—sometimes as little as $500,000 in an initial financing—in first and second rounds.

They have picked several winners among the numerous companies attempting to make cardiovascular therapies less traumatic. In addition to Advanced Cardiovascular Systems, they backed Devices for Vascular Intervention, a maker of a catheter-based means of removing arterial plaque, and CardioThoracic Systems, which developed tools used to perform coronary artery-bypass surgery on a beating heart. Eli Lilly acquired Devices for Vascular Intervention in 1989, and later spun it out in the creation of Guidant. Guidant bought CardioThoracic Systems in 1999.

Such devices remain a focus for USVP, reflecting the experience of partners such as Mr. Kaganov, who led Boston Scientific's business-development efforts before joining the firm in 1996.

While much of the attention in cardiovascular market of late has centered on coronary-artery disease, USVP has focused on what it sees as emerging and far less-competitive field: peripheral vascular diseases, such as blockages that occur in arteries serving the arms and legs.

One of its bets in this field is **CryoVascular Systems,** which it first backed in a 1998 Series A. The Los Gatos, Calif., company's catheter and angioplasty device clears blocked arteries and uses extreme cold, or "cryoplasty," to lessen the wound-healing response that can cause angioplasty-treated vessels to grow clogged from the spread of smooth-muscle cells.

As the balloon expands, a burst of liquid nitrous oxide cools the balloon to about minus 10 degrees Celsius, inducing smooth-muscle cells to kill themselves. CryoVascular sells the system through partner Boston Scientific, which obtained distribution rights in a 2003 deal in which it made an equity investment in CryoVascular and gained the right to acquire the company.

CryoVascular initially targeted the coronary market but shifted to the peripheral sector in early 2002. "They didn't drive the decision, but they were proactive contributors to it," said CEO Jeffrey G. Gold. "USVP was pivotal to the evolution of the company."

Though 12 million people in the United States suffer from blocked peripheral arteries, corporations have only recently recognized the field's potential, observers said. Technologies that have been effective for coronary-artery disease, angioplasty and drug-eluting stents, offer relatively little benefit outside the heart. This limited the number of patients who were actually treated.

With the introduction of new technologies, that is changing. With patients seeking solutions offered by companies like CryoVascular, whose system earned approval in 2002, and FoxHollow Technologies, which makes a catheter-based system for removing arterial plaque, corporations are following the market more closely, Mr. Kaganov said. "We were fortu-

U.S. Venture Partners

MAIN OFFICE

2735 Sand Hill Rd., Menlo Park, CA 94025
Phone: (650) 854-9080 | Fax: (650) 854-3018 | www.usvp.com

KEY PERSONNEL

William K. Bowes Jr. | Founding Partner
Dr. Jonathan D. Root | **Philip M. Young** | General Partners
Alan L. Kaganov | Partner
Casper de Clercq | Venture Partner

nate to have seen that five years ago," he said. While a backer of CryoVascular, USVP did not invest in FoxHollow.

As early-stage investors, the partners do not shy from helping entrepreneurs set their company's strategy and direction. Mr. Gold described Dr. Root, who sits on the CryoVascular board along with Mr. Kaganov, as someone who challenges, in a constructive way, the thinking of management.

Hugh R. Sharkey, CEO of **CardioKinetix,** a portfolio company in Redwood City, Calif., described Mr. Kaganov as similarly active. "He's very involved, if anything more involved than I'd like to see as a board member, but that's his style, and it should be a reassurance to" USVP's limited partners, he said.

CardioKinetix, which raised a $6.3 million first round in May from USVP, **JPMorgan Partners** and angel investors, represents one of the firm's latest attempts at making cardiovascular treatments less invasive. The company's device would address ventricular remodeling, which occurs when a heart attack destroys a section of the heart, robbing it of its ability to pump effectively. The condition is the primary cause of congestive heart failure.

Unlike other heart-failure devices in development, the CardioKinetix product would be delivered through a catheter, Mr. Sharkey said.

The consistency of USVP's strategy is even more pronounced on the biotech side. While other firms have favored in-licensing companies, USVP continues to back startups that discover their own compounds. Though licensing approved products promises early revenue, Dr. Root said he is unimpressed with the long-term prospects of most specialty pharmaceutical companies.

"When you obtain that molecule, you can assume you were the highest bidder," he said. "That's just not a sound business proposition."

The strategy means that USVP did not see a parade of portfolio companies go public last year, as some firms did. Over time, however, drug discovers are better positioned to fill their own pipelines and to capitalize on pharmaceutical companies' need for products, Dr. Root said.

USVP uses two strategies to reduce the risk of early-stage investing. First, it takes only one major risk per company, betting either on an unproven drug candidate or an unproven drug target. South San Francisco-based **Proteolix,** for example, is developing drugs targeting proteins found in the proteasome, which is part of the cell's system for degrading proteins. The 2003 introduction of Velcade, a proteasome inhibitor developed by Millennium Pharmaceuticals, proved this mechanism can be targeted effectively. This made the firm comfortable in betting on Proteolix's new drug candidates.

The firm also strives to build syndicates of firms willing to support a company through tough periods. It took this approach with Proteolix, teaming up with **Advanced Technology Ventures, Latterell Venture Partners, Vertical Group** and **Genentech** to fund the company's $10.5 million first round in December of 2003.

It did the same with **Raven Biotechnologies,** and monoclonal antibody company the firm first funded in a $20.7 first-round in December of 2000, leading a syndicate that included **CMEA Ventures, Hambrecht & Quist Capital Management** and **Milepost Ventures.** Each of them returned to back Raven's $40.8 million second round two years later.

USVP in recent years has brought aboard younger members to prepare for an eventual succession of leadership. After deciding last year to continue devoting 25 percent of their capital to health care, they sought to strengthen their health care team by hiring a new venture partner, entrepreneur Casper de Clercq.

Mr. de Clercq in 1999 co-founded Epicor Medical, which St. Jude Medical acquired last year to gain access to the company's surgical treatment for atrial fibrillation. Mr. de Clercq also had formerly worked for one of USVP's portfolio companies, Aerogen, a drug-delivery company that went public 2000.

With the addition of Mr. de Clercq, who, like Dr. Root is in his 40s, the firm has younger members to complement Messrs. Young and Kaganov, who are both in their 60s. "Our partnership has the right combination of long-term, midrange and next-generation" experience, Mr. Kaganov said.

Investment Snapshot *

Companies Backed	**29**
Companies Private	18
Companies Taken Public	3
Companies Acquired	5
Companies Out of Business	3

Breakdown by Sector		**Breakdown by Rounds**	
Health Care Services	0	Seed	1
Medical Software	4	First Round	18
Biopharmaceuticals	9	Second Round	20
Medical Devices	16	Later Stage	17

Minimum Investment $500,000

Maximum Investment Per Company $15 million

Number of Investments in 2004 7

Current Fund U.S. Venture Partners IX, L.P., $600 million

* Only health care investments made since Jan. 1, 1997.

Sources: VentureOne