SD's venture scene strong but not without pitfalls

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The key takeaway from San Diego Venture Group's 2015
Venture Outlook is that the region has been performing fairly well by most measures compared to the overall venture capital industry, though there have been several downward trends over the last decade to keep an eye on.

David Coats, founder and managing director of **Correlation Ventures**, shared some data that's never been publicly released before from the firm's self-proclaimed most complete database of the U.S. venture capital market, which he said contains 98 percent of all VC financings since 1987.

Based on this data, San Diego companies have received about 5 percent of all the venture capital money that has been invested into U.S. companies over the last decade -- $12 billion of the $242 billion total. That figure hit 6 percent in 2013 after falling to a low of 3 percent from 2007 through 2009.

And San Diego puts that money to work better than the industry as a whole. San Diego companies produced an average realized return for venture firms of 1.9 times investment, compared to the industry average of 1.7 times over the last decade. "Perhaps this is within the margin of error, but I'm calling it a win for San Diego," Coats said.

That number hit three times investment in 2013 in San Diego, but the industry average has been catching up.

"If you look at the graph a little closer, there is a warning sign there though," Coats said. "Our outperformance occurred primarily during the first half of the decade, and we underperformed slightly during the second half."

San Diego deals in the top 10 percentile based on valuation also outperformed the industry, with a 4.5 times average over the last decade compared to a nationwide four times rate. Coats said this would be reversed when it comes to the top 1 percent of deals, since San Diego's market doesn't have many huge winners like **Facebook Inc**. (Nasdaq: FB) or **Twitter Inc**. (NYSE: TWTR).

Another warning sign for San Diego is the region's low capital efficiency, or amount required and raised by firms seeking VC money. This can be explained, in part, by the region's unusually high concentration of biopharmaceutical companies, with 42 percent of all capital over the last decade going to this sector compared to 15 percent industry-wide.

"Last decade the average San Diego company raised $38 million prior to exit, compared to the industry average of $26 million -- and that difference has grown over the last decade," Coats said.

When they do exit, San Diego companies' values are, on average, less than the overall industry's at $94 million compared to $104 million, though Coats said when looking at only the top 10 percent of exits, San Diego actually beats the nationwide figure with $315 million compared to $240 million.

Interestingly, San Diego's VC-backed exiting companies went public at a rate two times the industry average, at 12 percent during the last decade. Venture-funded firms that went out of business account for 43 percent of all exits in San Diego, compared to 40 percent nationwide.

Perhaps the most concerning data point deals with dollars raised: while $33 billion was raised industry-wide in 2014 — nearly double that of 2013 — Coats said San Diego-based VC firms accounted for very little of that.

A panel of VCs discussed several additional trends in the venture space and debated whether 2015 will see the busting of the industry's third bubble — check back tomorrow for a recap of that discussion.

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