

Nashville Venture Capital Report

2005 - 2015



Presented by



NASHVILLE
HEALTH CARE
COUNCIL

With special thanks to Launch Tennessee for its contribution of data

NASHVILLE VENTURE CAPITAL REPORT

2005-2015

Executive Summary

Welcome to the second edition of Nashville Venture Capital Report. This report provides a detailed look at the growth of the venture capital industry in Nashville from 2005 through 2015, with a special focus on venture capital investment in Nashville's health care industry. The data in this report builds on the themes detailed in the first edition and provides credence to those who cite Nashville as a growing venture capital hub and one of the leading health care markets in the United States. Some of the key findings of this edition of the study are outlined below.

- Since the beginning of 2005, more than \$1.6 billion of venture capital investment have been received by over 300 different Nashville-based companies (**Figure i**).
- More than \$940 million was invested in Nashville health care companies by venture capital firms from 2005 through 2015. This amounts to almost 60% of Nashville's total venture capital investment dollars over that time period.
- Since 2009, annual venture capital investments in Nashville have grown to 450% the 2009 level (**Figure ii**). This growth in investments well exceeded that of the national venture capital market, where annual venture capital investments grew to only 140% the 2009 level.
- Venture capital investment in Nashville Health Care IT companies grew from \$2 million in 2009 to a peak of \$62.5 million in 2014. Venture

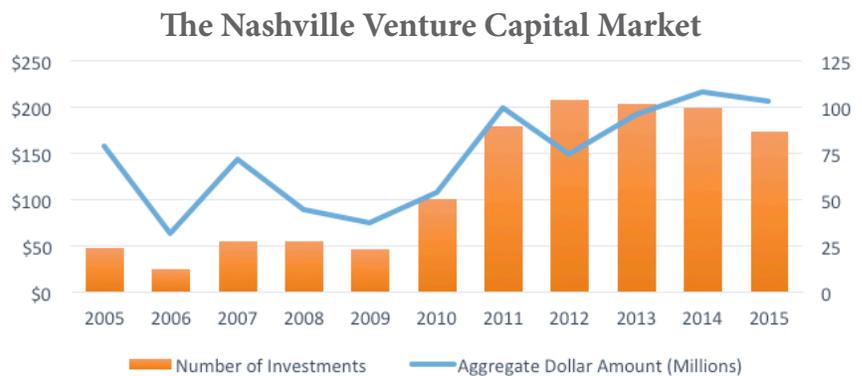


Figure i: Overview of Nashville Venture Capital Market

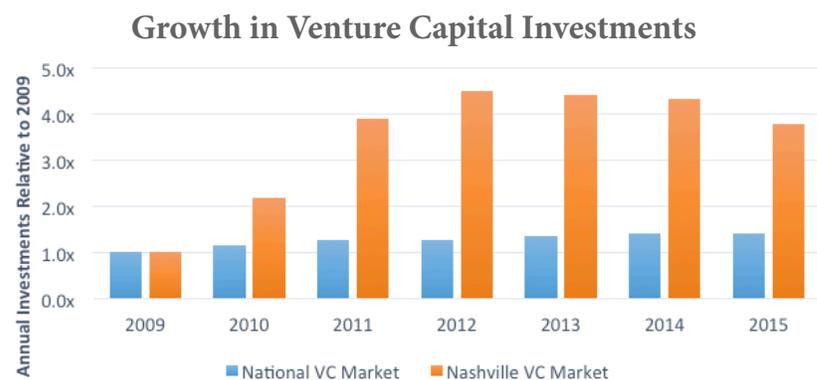


Figure ii: Comparison of Nashville and National Venture Capital Investments

investment in Health Care IT companies surpassed that of Health Care Services companies in 2012 and now represents the largest share of venture capital investments in Nashville health care companies (**Figure iii**).

- The increased seed-stage investment activity from 2011 - 2013 has resulted in more companies seeking, and ultimately receiving, early-stage and growth capital in 2014 and 2015 (**Figure iv**). This has, in turn, resulted in an \$87 million increase in growth-stage investments relative to the approximate \$58 million amount in 2009.
- Support from local investors is necessary to continue Nashville's momentum from the previous 5 years. Out of the 28 companies that received growth capital investments in 2014 - 2015, 18 received an earlier round of seed/early-stage financing. In every one of these earlier financings, local individuals and firms were the primary investor.

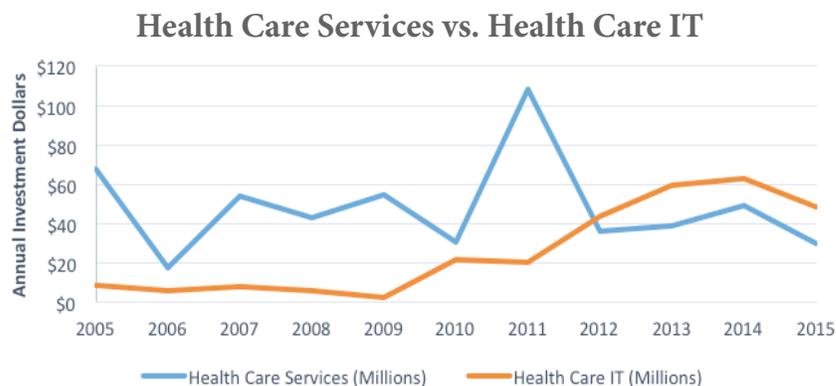


Figure iii: Comparison of Health Care Services and Health Care IT Investment

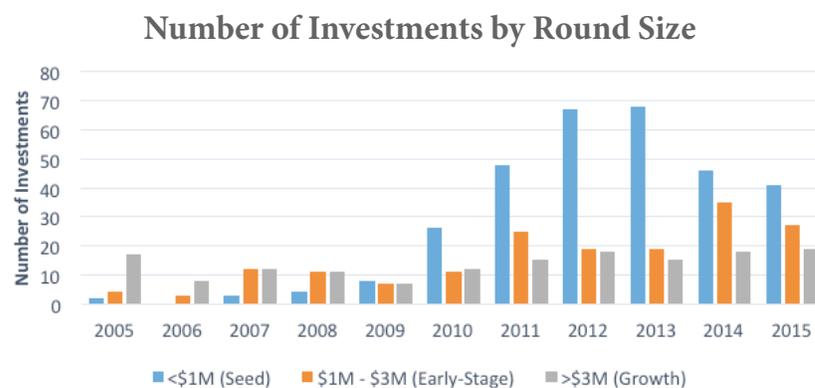


Figure iv: Number of Nashville Venture Capital Investments by Round Size

Welcome to the Nashville Venture Capital Report

On behalf of Nashville Capital Network (NCN) and the Nashville Health Care Council (the Council), we are proud to present the second edition of the Nashville Venture Capital Report. The primary goal of this report is to provide to all stakeholders of the venture capital and health care communities a comprehensive resource that offers valuable insight into Nashville's venture capital activity over the past 11 years.

Nashville is widely considered to be one of the nation's leading health care markets. From its beginnings, namely with the founding of Hospital Corporation of America in 1968, the city's health care industry has grown to include more than 400 diverse health care companies, creating more than 250,000 jobs in the community and a \$38.8 billion economic benefit to the area. Due to the dynamic changes occurring in health care, new health care companies are being founded in Nashville at a faster rate than ever before. These innovative new companies are forming partnerships with the city's health care community to address the new and evolving challenges brought about by the transforming regulatory landscape and the pressing need for cost and quality improvements in the U.S. health care system.

As this report highlights, from 2005 through 2015, venture capital firms have invested more than \$1.6 billion in over 300 Nashville-based companies. In addition, this report illustrates a continuation of the growth trend in Nashville venture capital activity shown in the first edition, which covered the time period from 2001 – 2011. With this second edition, we hope to further highlight the evolving venture capital industry in Nashville. Furthermore, we hope that this report will illustrate the important roles that venture capital and health care play in helping to make Nashville an elite city for entrepreneurship.

Sid Chambless, Executive Director, Nashville Capital Network
Hayley Hovious, President, Nashville Health Care Council



Local Infrastructure

HEALTH CARE INDUSTRY

Home to a dynamic community of more than 400 health care companies, Nashville is a one-of-a-kind center of innovation. With a rich tradition of entrepreneurship and executive talent, Nashville has shaped the nation's health care landscape over the past five decades and continues to improve the delivery of patient care across the globe.

Not only a well-known center of hospital management, Nashville is home to leading companies in a diverse range of sectors, including ambulatory and outpatient surgery, long-term care, behavioral health, population health, academic research, and health information technology.

The city is headquarters to such industry leaders as Acadia Healthcare, AMSURG, Brookdale Senior Living, Community Health Systems, HCA, and LifePoint Health, among many others. Additionally, more than 400 health-care-focused professional service firms in Nashville provide deep health care expertise. The 18 publicly traded health care companies located in Nashville have a combined employment of 500,000 and \$73 billion in annual revenue.

LOCAL ECONOMY

According to the U.S. Bureau of Labor Statistics, over the past 12 months, the Nashville MSA has experienced the 18th fastest growth rate in employment among the 51 large metropolitan areas with more than one million residents. The Nashville MSA also now has the second lowest unemployment rate among these metros, at 3.0 percent.

Nashville has a reputation for being an ideal business location and is home to many large corporate headquarters, such as those of HCA Holdings, Nissan North America, Tractor Supply Co., Asurion, and Dollar General. Nashville also offers employees a high quality of life and a lower cost of living than national averages, all of which have garnered the city the following accolades from major publications in recent years:

- #4 Best City for Job Growth, Forbes, May 2016
- #8 City People Are Moving to Right Now, Realtor.com, June 2016
- #6 Best City to Start a Business, Inc. Magazine, August 2015
- #4 Top City for Millennial Entrepreneurs, Thumbtack.com, September 2015
- #9 Up-and-Coming Cities for Tech Jobs, ZipRecruiter, July 2015
- Top Ten City for Growth and Prosperity, Brookings Institution, February 2016

A Deep Look at Nashville's Venture Capital Industry

The first edition of this report, which was published in August 2012, included data collected by NCN and the Council through surveys of a number of venture capital firms. These firms provided the company names, financing amounts, industry sectors, number of unique financing events, and stages of Nashville investments from 2001 – 2011. Pitchbook and the Moneytree™ Report were also consulted, along with NCN's internal database, to complete the dataset. Venture capital investment data obtained since the first edition of this report was compiled by LaunchTN, a public-private partnership focused on supporting the development of high-growth companies in Tennessee. While data as far back as 2001 has been accumulated, this report focuses on the time period from 2005 through 2015.

In order to limit the focus of this report to venture capital activity, the following were excluded: leveraged buyouts, dividend recapitalizations, mezzanine debt offerings, distressed investments, and equity investments in larger or more established companies deemed to be mature. Furthermore, this report adopts LaunchTN's definition for venture funding (as of 2015), which excludes investments in excess of \$25 million unless a qualifying venture investment in the company occurred prior to that round.

The dataset obtained for the first edition of this report did not necessarily contain equivalent data points or definition conventions with respect to the dataset obtained from LaunchTN. As such, this report has excluded some of the data points from the first edition and has adopted a modified convention to categorize funding stages. For discussion purposes in this report, the naming conventions in **Table 1** are adopted for the corresponding investment round sizes.

Table 1: Round Size Classification

Round Size	Classification
Less than \$1 million	Seed
\$1 million - \$3 million	Early-Stage
Greater than \$3 million	Growth

While investment rounds less than \$1 million are considered “seed-stage” in this report, this does not preclude follow-on investment rounds of less than \$1 million from also being classified as “seed-stage.”

With the previously mentioned exclusions and conventions, Nashville-based companies that accepted capital in return for an equity stake were analyzed. The process presented an accurate depiction of venture capital activity in Nashville and is a continuation of the most comprehensive data set ever compiled on the city's venture capital industry. All contributors proved to be invaluable resources in collecting the necessary data for this study.

A Broad Overview of the Nashville Venture Capital Market

Figure 1 provides a broad summary of the number of annual venture capital investments, and annual aggregate dollar amounts, received by Nashville companies from 2005 through 2015. The years prior to 2010 were characterized by 26 or fewer annual investments totaling between \$62 million and \$160 million. Overall, no distinct growth trends are evident in the data prior to 2009.

Years 2005 through 2007 included several isolated, large investment rounds that resulted in elevated average round sizes for those years (**Figure 2**). As such, aggregate investment dollars were higher than typical for those years, relative to the corresponding number of investments.

Beginning in 2010, the number of annual venture investments in Nashville accelerated sharply (**Figure 2**). Annual investments peaked in 2012 at 104, which was 360% higher than the average number of investments between 2005 and 2009. The majority of the growth in annual investments was composed of seed-stage investments (**Figure 3**).

Several local and macro factors likely contributed to the significant growth in seed-stage financings in Nashville. The TNInvestco program, which was established in 2009, allocated approximately \$200 million of tax credits for deployment into local seed- and early-stage companies. The deployment period for the TNInvestco funds generally ran from 2010 to 2015, which

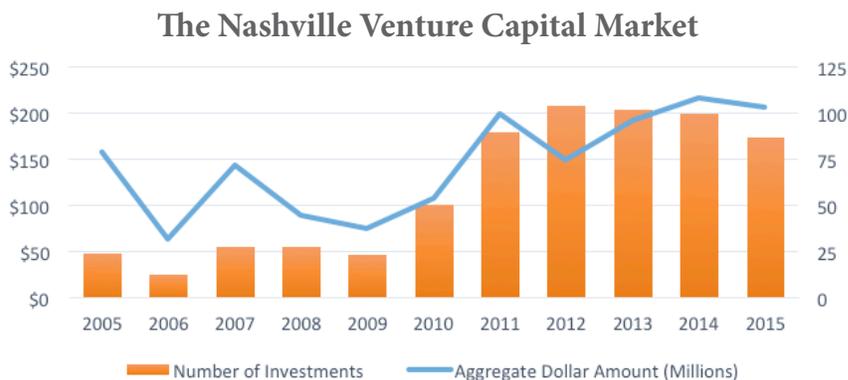


Figure 1: Overview of Nashville Venture Capital Market

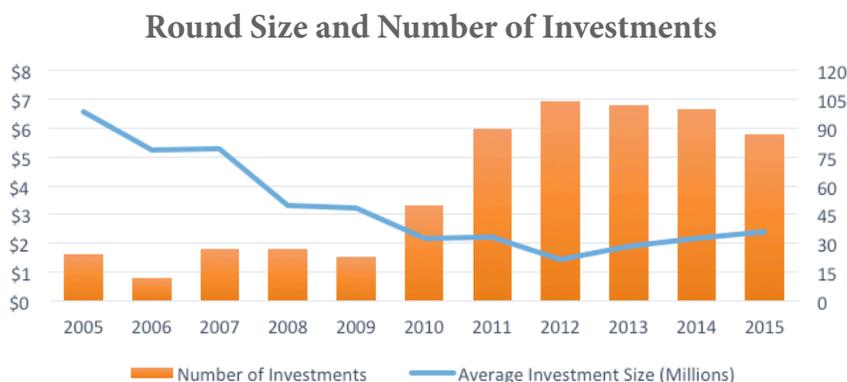


Figure 2: Round Size and Number of Investments for Nashville Venture Capital Market

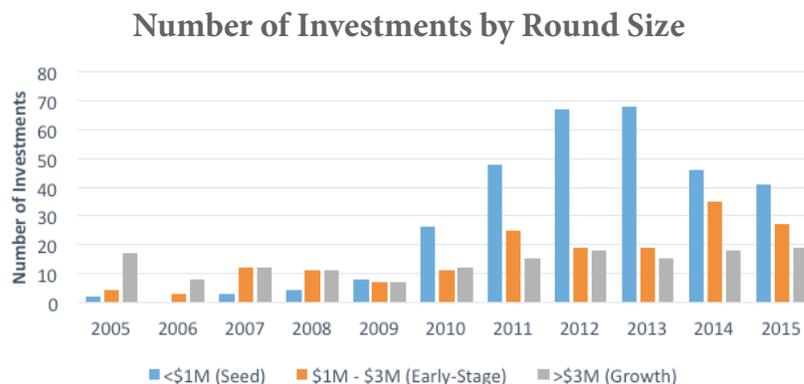


Figure 3: Number of Nashville Venture Investments by Round Size

coincides with the recent peak of seed investments in Nashville. Improving economic conditions led to increased participation in private investing by local angel investors, who typically invest in seed-stage companies. In addition, local initiatives such as the Nashville Entrepreneur Center and other accelerator programs increased the accessibility of mentorship and seed capital for Nashville startups.

The acceleration in seed-stage investments that began in 2009 has led to an increase in early-stage and growth capital investments for the most promising companies, particularly during the most recent years of this study. Relative to 2009, the number of annual early-stage investment rounds has increased by up to 400%, and the number of annual growth capital rounds has increased by approximately 170%.

While growth in the number of seed-stage investments was significantly higher than that of early-stage and growth capital investments, the resulting growth in investment dollars has been far more significant for non-seed investments (**Figure 4**). From 2009 through 2015, annual early-stage investment dollars grew by approximately \$49 million at its peak, and annual growth investment dollars increased by almost \$87 million. These quantities are relative to peak growth of \$15 million in annual seed-stage investment dollars.

After a steady decline in the average size of venture capital investment rounds in Nashville,

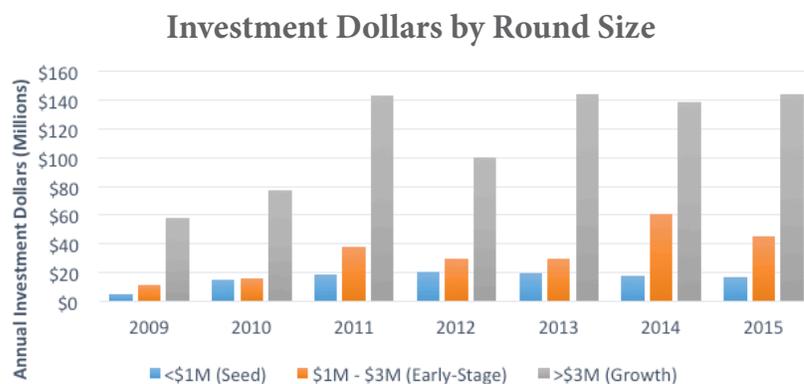


Figure 4: Annual Investment Dollars by Round Size for Nashville VC Market

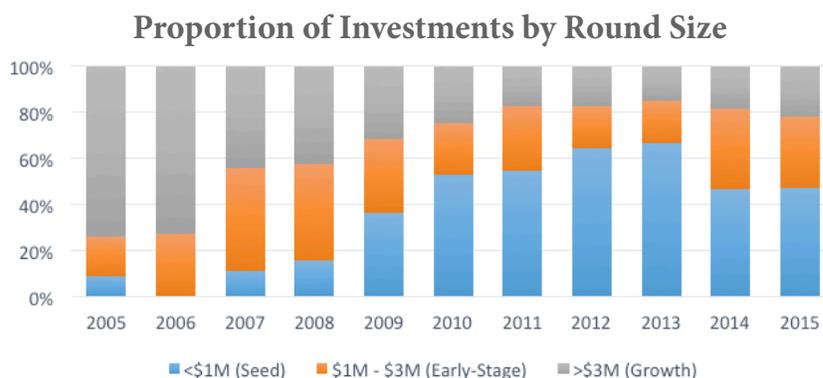


Figure 5: Proportion of Annual Venture Investments by Round Size

the average investment size has now grown at an 18% compound annual growth rate since 2012 (Figure 2). This growth is indicative of seed-stage companies graduating to the early-stage and growth phases, during which the companies can attract larger round sizes to achieve significant revenue growth.

As shown in **Figure 5**, early-stage and growth capital rounds as a percentage of total annual rounds bottomed in 2012-2013 and increased afterward. In 2014, non-seed-stage investments

reached 54% of total rounds, the most since 2009. During that year, Nashville companies received 35 early-stage investments, which surpassed all other years in this study. In 2015, Nashville companies attracted a record 19 growth capital rounds. These recent trends over the last two years of the study more closely resemble the “funnel-shaped” capital continuum one would expect to see in a thriving early-stage ecosystem (see years 2014 and 2015 in Figure 3 for a representative “funnel-shaped” continuum).

A Comparison with National Venture Capital Trends

The data in **Figure 6** supports the characterization of Nashville as an emerging and dynamic market for venture capital activity. National data was obtained from the Moneytree™ Report, which is not necessarily directly comparable to the in-depth sourcing of Nashville data used in this study. However, growth trends between the two datasets are comparable and show that Nashville's venture capital activity is accelerating much more rapidly than that of the national market. Since 2009, growth in Nashville venture capital investment rounds, which peaked at 4.5 times the 2009 level, has well exceeded that of the national market, where the number of annual venture capital investments grew to only 1.4 times the 2009 level.

Nashville has also experienced impressive growth in annual venture capital investment dollars relative to its 2009 level (**Figure 7**), albeit not at the same rate of growth as annual investment rounds. The lower growth in annual dollars relative to that of annual investments is indicative of the active seed-stage ecosystem that emerged in Nashville after 2009.

When comparing the Nashville and national markets, Nashville's growth in yearly aggregate investment dollars relative to its 2009 level has exceeded that of the national market in five out of the last six years. However, during the last two years of the study, the National market's growth relative to its 2009 level is more comparable to that of Nashville's.

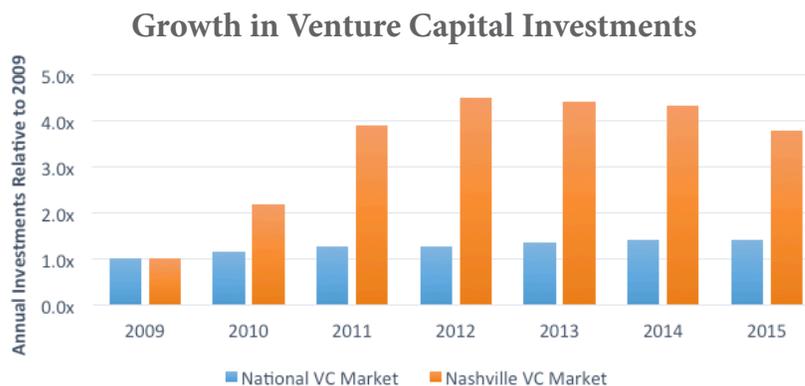


Figure 6: Comparison of Nashville and National Venture Capital Investments

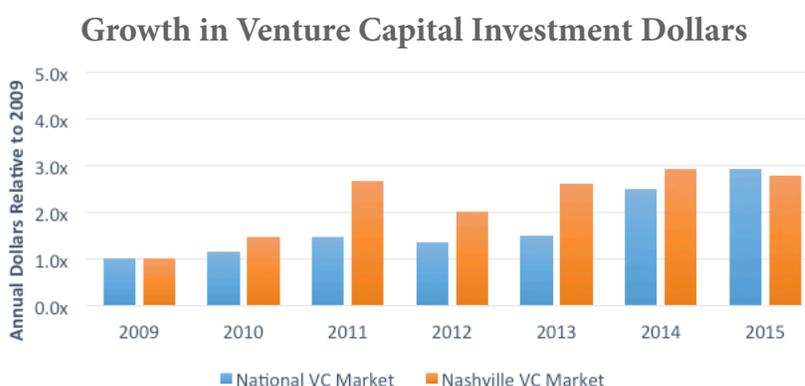


Figure 7: Comparison of Nashville and National Venture Capital Investment Dollars

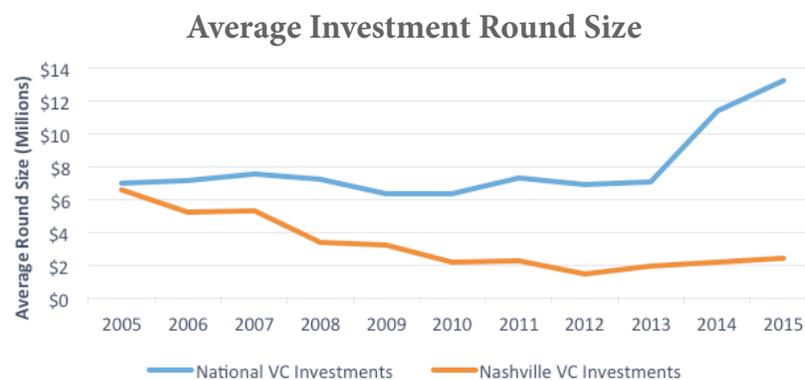


Figure 8: Average Investment Round Size for Nashville and National Venture Capital Markets

The national market's growth over the last two years of the study can be attributed in part to a national focus on large, later-stage investment rounds, which skewed the national average round size

and total funding higher during those two years (**Figure 8**). Relative to the 2013 level, the national average investment size increased by 62% and 89% in 2014 and 2015, respectively.

Health Care Industry Trends

For discussion purposes in this study, the health care industry is composed of the following sub-categories: Health Care Services, Health Care IT, Medical Devices, and Biotech. In terms of aggregate venture capital dollars received by Nashville companies, the health care industry exceeds all others combined (**Figure 9**). From 2005 through 2015, health care investment dollars have composed almost 60% of total venture capital investment in Nashville. Based on data from the 11 years of this study, health care companies in Nashville received an average of approximately 26 investments totaling over \$85 million from venture capital firms each year. In total, venture capital firms invested over \$940 million into Nashville health care ventures from 2005 through 2015.

In the first edition of this report, Health Care Services companies had attracted the most venture capital dollars of the health care cohort. In 2011, venture investments in Health Care Services companies peaked at 20 investments totaling \$108 million. However, the trend in Health Care Services investments returned to normative levels after 2011 (**Figure 10**).

After minimal funding during the 5 years prior to 2010, Nashville Health Care IT companies received increased venture investment activity over the last six years of this study (**Figure 11**). Investment in Health Care IT companies surpassed funding in Health Care Services companies, in terms of aggregate

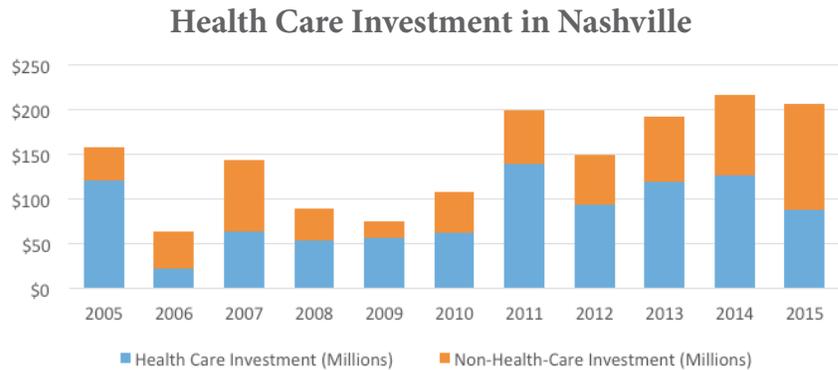


Figure 9: Overview of Health Care and Non-Health-Care Investment in Nashville

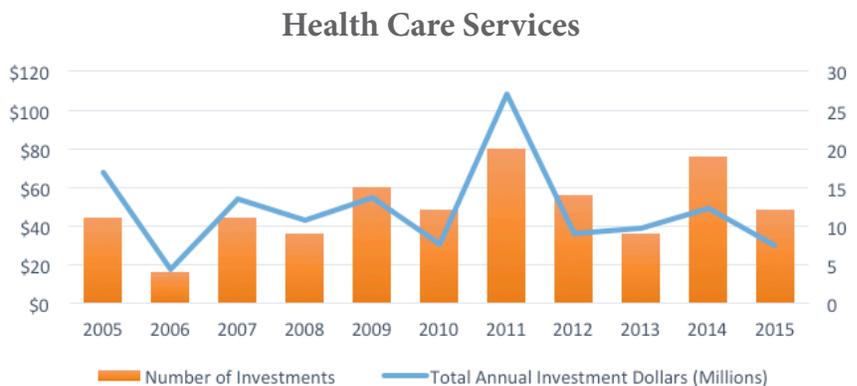


Figure 10: Venture Capital Investment in Nashville Health Care Services Companies

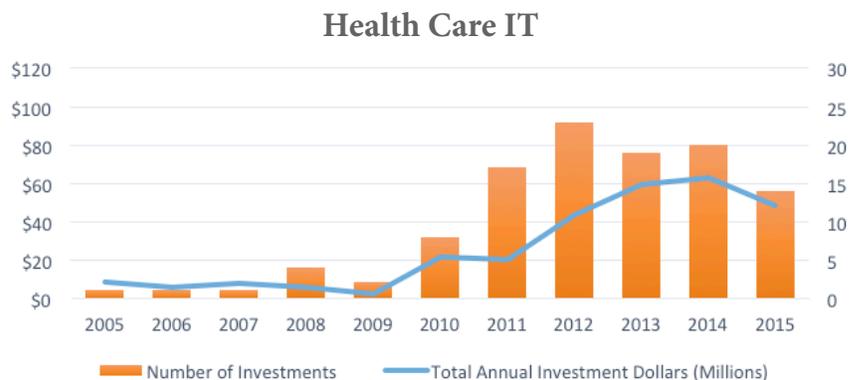


Figure 11: Venture Capital Investment in Nashville Health Care IT Companies

dollars and number of deals, for years 2012 through 2015. The timeframe of this growth trend in Health Care IT investment correlates with the enactment of the Health Information Technology for Economic and Clinical Health (HITECH) Act in 2009, which created financial incentives to “promote the adoption and meaningful use of health information technology.”

In general, venture investment in Biotech and Medical Devices companies has remained suppressed, relative to the remainder of the health care cohort, throughout the timeframe applicable to this study. Biotech companies had an isolated year of significant funding in 2005, receiving \$38 million in one investment round, but remained suppressed through 2009 (Figure 12). After 2009, Biotech companies experienced an accelerating trend in funding that peaked in 2013 at nine investments totaling \$19.5 million. Venture investment in Medical Devices companies did not exhibit any significant growth trends or isolated years of outsized funding over the timeframe applicable to this study (Figure 13).

Other Industry Trends

In addition to the health care industry, several other industries are thriving in Nashville. Since 2005, more than \$655 million of venture capital funding has been invested in sectors other than health care. In the most recent year of this study, non-health-care (NH) companies received more investment dollars than health

care companies for the first time since 2007 (Figure 9).

Venture capital investment in Nashville NH companies has traditionally been dominated by Technology / Business Services companies. Growth in investment dollars for these companies has generally been accelerating since

the beginning of 2010 (Figure 14). In 2015, venture capital investments in Technology / Business Services companies composed over 60% of NH investment dollars and over 35% of total invested dollars.

Venture capital investments in Media/Internet companies

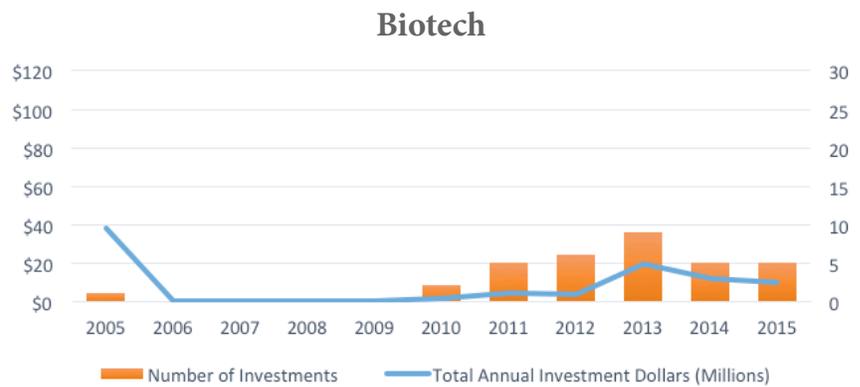


Figure 12: Venture Capital Investment in Nashville Biotech Companies

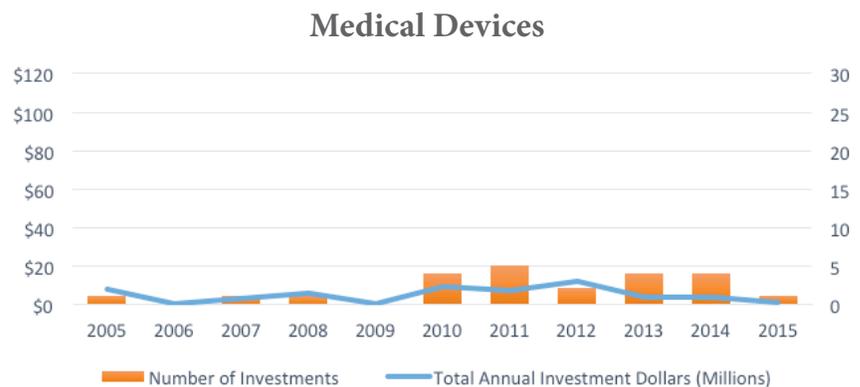


Figure 13: Venture Capital Investment in Nashville Medical Devices Companies

gained momentum after 2009. However, investment in these companies peaked in 2013 at 23 investments totaling over \$31 million (Figure 15). This category has since experienced diminished levels of investment in terms of aggregate dollars and number of investments.

Prior to 2009, Technology/Hardware (Figure 16) and Retail (Figure 17) companies have respectively accounted for less than 10% of overall NH venture capital investment dollars. Growth in venture capital dollars invested

and number of investments accelerated for Technology/Hardware companies in 2014 and 2015. As a result, Technology/Hardware represented approximately 15% of total NH venture investment dollars in 2015, up from 5% in 2013 and 6% in 2014. Telecommunications startups received significant levels of investment during the early part of this study but have since experienced diminished levels of investment (Figure 18).

As evidence of the growing diversity in Nashville's

entrepreneurial environment, growth in investments received by companies not fitting within one of this report's main categories (i.e., Other), including educational facilities, restaurants, breweries, and many other types of businesses, has accelerated since 2011 (Figure 19). In the latest year of this study, venture capital investments in companies fitting the Other designation represented 14% of total dollars, and over 30% of rounds, invested in NH companies.

Technology/Business Services



Figure 14: Venture Capital Investment in Nashville Technology/Business Services Companies

Media/Internet

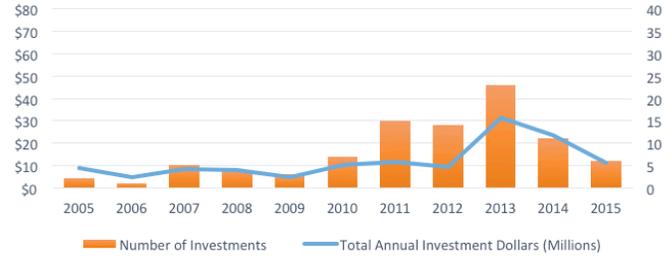


Figure 15: Venture Capital Investment in Nashville Media/Internet Companies

Technology/Hardware

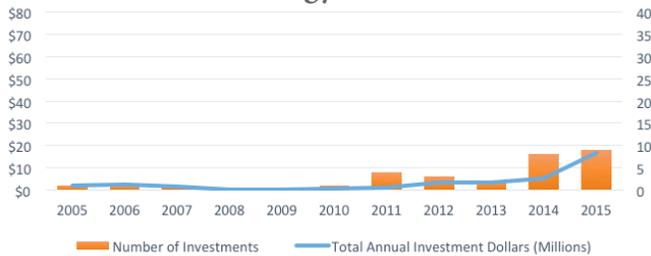


Figure 16: Venture Capital Investment in Nashville Technology/Hardware Companies

Retail

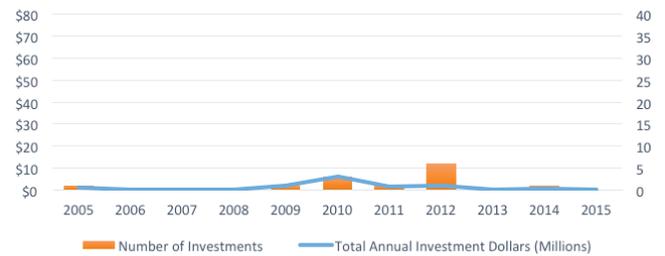


Figure 17: Venture Capital Investment in Nashville Retail Companies

Telecommunications



Figure 18: Venture Capital Investment in Nashville Telecommunications Companies

Other

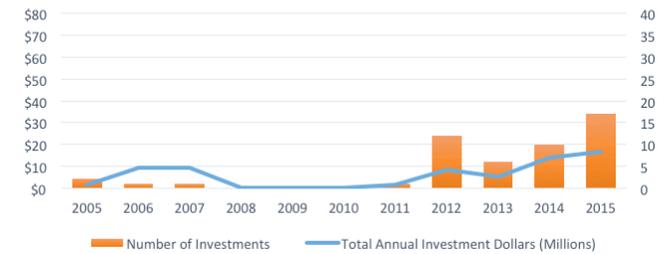


Figure 19: Venture Capital Investment in "Other" Nashville Companies

Successful Exits

The intent of this study was to track investments rather than exits in the venture capital industry. However, the research did uncover several noteworthy exits since the first edition of this report was published. This study does not include any information regarding the returns associated with these exits; however, the representative exits shown in **Figure 20** do indicate that Nashville's venture capital activity and infrastructure are supportive of high-profile, large-scale success by Nashville companies.

 <p>Transaction: Acquired for \$50M by Provista LLC</p> <p>Firms Involved: Nashville Capital Network River Cities Capital Funds</p>	 <p>Transaction: \$75M Initial Public Offering</p> <p>Firms Involved: Private Investors</p>	 <p>Transaction: Acquired for \$75.5M by Almost Family</p> <p>Firms Involved: Fulcrum Ventures Gemino Healthcare Finance Prudent Capital</p>
 <p>Transaction: Acquired for \$185M by Emdeon</p> <p>Firms Involved: HLM Venture Partners Mitsui & Co. Noro-Moseley Partners Solidus Sandbox Industries West Health Investment Fund</p>	 <p>Transaction: Acquired for \$195M by Kindred Healthcare</p> <p>Firms Involved: Pacific Venture Group River Cities Capital Funds Sterling Partners Three Arch Partners</p>	 <p>Transaction: Acquired for \$333M by Wright Medical Group</p> <p>Firms Involved: Axiom Ventures InterWest Partners MB Venture Partners Noro-Moseley Partners</p>
 <p>Transaction: Acquired for \$357M by Cardinal Health</p> <p>Firms Involved: Ascension Ventures Blue Cross Blue Shield Sandbox Industries Welsh, Carson, Anderson & Stowe</p>	 <p>Transaction: Acquired for \$850M by Experian</p> <p>Firms Involved: CB Health Ventures Dauphin Capital Partners Greenfield Capital Partners SSM Partners</p>	 <p>Transaction: Acquired for \$3.8B by Cigna Corp.</p> <p>Firms Involved: Private Investors GTCR</p>

Figure 20: Representative Exits of Nashville-Based Companies That Received Venture Capital

Venture Capital Investment: An Opportunity

As discussed previously in this report, growth in seed-stage investments has increased dramatically since the beginning of 2010. Improved economic conditions, the TNInvestco program, the Incite Program, and local initiatives such as the Nashville Entrepreneur Center have contributed to the availability of local seed-stage capital for new ventures. On the other end of the continuum, Nashville companies have demonstrated the ability to attract later-stage growth capital from both local and outside venture capital firms. Numerous firms that previously had not invested in Nashville appeared in the data in the most recent years of this study. Over the past several years in particular, regional and national venture capital firms have shown an increased willingness to invest in the growth rounds of Nashville companies once the companies have surpassed significant revenue and profit milestones.

However, outside venture capital firms have not yet demonstrated a consistent appetite for investing in the earlier stages of Nashville companies. The extra attention from growth-stage venture firms, combined with the increased availability of local seed-stage capital, has created an apparent capital gap at the early-stage level. This gap, which shows up most clearly in the data in 2012 and 2013 (Figure 3), can become an impediment to a healthy capital continuum without proper attention.

This evolving dynamic presents an exciting opportunity for Nashville investors. Hiring costs, pursuit of growth opportunities, and other factors often increase a company's capital requirements in the early-stage rounds beyond the scope of individual angel investors. Therefore, local venture resources focusing on the early-stage rounds are imperative to maintaining a healthy capital continuum in Nashville. Out of the 28 companies that received growth capital investments in 2014 – 2015, 18 received an earlier round of seed/early-stage financing. In every one of these earlier financings, local individuals and firms were the primary investors.

As shown in the data in 2014 and 2015 (Figure 3), local firms such as NCN have done a commendable job of fulfilling the early-stage capital gap, which has resulted in an elevated number of companies receiving growth capital (from 2012 through 2015, NCN led early rounds for 25% of the Nashville-based companies that ultimately raised \$3 million or more). However, a continual effort by local investors will be required to build upon this progress and ensure that the most promising companies in Nashville have the capital resources to continue to navigate the gap in the continuum.

Continuing Nashville's Progress

The data from this study indicates that Nashville's community leaders and private investors have worked together to develop a robust and thriving entrepreneurial ecosystem. The city's early-stage capital resources have evolved greatly since the first edition of our study, and many of the components required for a healthy, sustainable ecosystem are now in place. New health care ventures continue to be a driving force in this ecosystem and are leading the way in capturing the attention of regional and national investors. While the data over the last decade illustrates Nashville's impressive growth, it is important that the city's constituents maintain this momentum.

To maintain this momentum, Nashville's brightest entrepreneurs will need continued access to capital to launch, build, and grow their businesses. Local investors have a great opportunity to support the most promising of these ventures and to participate in transformational economic growth in Nashville for the years to come. This will in turn continue to strengthen Nashville's position as a leading market for health care and venture capital.



Nashville Capital Network

Nashville Capital Network is a network of 130 investors, most of whom have been founders and executives of Nashville's most successful companies. NCN leverages the experience and expertise of the individuals within the group to identify, develop, and support promising, high-growth companies. NCN manages several investment funds, including NCN Angel Fund I, NCN Angel Fund II, and Tennessee Angel Fund.

NASHVILLE HEALTH CARE COUNCIL

Nashville Health Care Council

The Nashville Health Care Council is a premier association of health care industry leaders working together to further establish Nashville's position as the nation's health care industry capital. Supported by nearly 300 corporate members, the Council serves as a trusted source for information on trends that influence the health care industry. The organization provides members with one-of-a-kind networking opportunities and access to Nashville's elite health care business community.

Jeffrey Hull – Author

Jeffrey Hull is an associate at Nashville Capital Network. He graduated from the University of Texas with a bachelor's degree in architectural engineering and a master's degree in civil engineering. Mr. Hull is currently a 2017 MBA candidate at the Owen Graduate School of Management, where he serves as President of the Vanderbilt Entrepreneur's Association. In addition to this study, Mr. Hull has co-published research on explosion damage for the American Society of Civil Engineers.