

Silicon Valley eyes long-awaited IPO resurgence

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By Phil Wahba and David Lawsky - Analysis

NEW YORK/SAN FRANCISCO (Reuters) - U.S. venture capitalists have had to contend with an IPO market that has been inhospitable -- but finally there are reasons to be optimistic a recovery could be around the corner.

On Thursday, venture-backed lithium-ion car battery maker A123 Systems Inc is set to debut on Nasdaq despite never having made a profit, in a test of how adventurous investors are.

A successful debut would suggest that investors are more willing to make risky bets, and open the door for a slew of venture-backed companies that have been waiting in the wings.

But no one is expecting a return to the dot-com days that produced 235 venture-backed IPOs in 2000. The more recent peaks of 97 venture-backed IPOs in 2004 and 86 in 2007 are more attainable, bankers say, and would mark a true comeback after only six such deals in 2008, and seven so far in 2009.

"A lot of those firms have been incubating. There's now an opportunity for them to go public," said Mark Hantho, global head of equity capital markets for Deutsche Bank. He did not think the IPO market will get "frothy" again any time soon, with stock markets only beginning to recover.

Many of the headline-grabbing IPOs this year have been backed by private equity firms, such as chipmaker Avago Technologies Ltd, owned in part by Kohlberg Kravis & Roberts, which raised \$745.2 million in August.

VC-backed IPOs -- typically for younger and riskier companies -- only accounted for 24 percent of total U.S. IPO proceeds so far in 2009, according to Thomson Reuters.

"The private equity deals in '05, '06, '07 tended to be larger, already profitable companies, so they've been able to tap into the market earlier" than venture-backed companies, said Lisa Carnoy, global head of equity capital markets at Bank of America Merrill Lynch.

Six of the seven IPOs this year with venture funding, such as online restaurant reservations system OpenTable Inc, are still trading above their IPO price, a performance that should draw investors.

"The pace of our dialogue with the VC community in Northern California has accelerated based on the success of five or six of the venture-backed IPOs so far this year," Carnoy said, adding that she expects activity will pick up in 2010.

SILICON VALLEY AWAKENS

Bankers, consultants and investors say the pulse of Silicon Valley has quickened but they understand that investors, though less risk averse than a year ago, still want companies that can prove they will grow and be profitable.

Dixon Doll, general partner of DCM Capital, said firms with recurring revenue are especially attractive, while investment banker Paul Deninger said past profitability also helps.

"The ideal IPO is a company that has four quarters of profitability," said Deninger, vice chairman of Jefferies and Co.

Thus, how well A123 will be received is a barometer for risk appetite since the battery maker has never made a profit.

In addition to A123, there are 17 venture-backed companies in the IPO pipeline, including university operator Education Management Corp and biotech concern Omeros Corp, both set to price next month.

"A pretty steady stock market is encouraging people sitting on the sidelines with cash," said Tracy Lefteroff, the global managing partner of PricewaterhouseCoopers venture capital practice.

But if capital markets stumble, public offerings by venture backed companies could be the first investors will shun.

"We're still early in the IPO market coming back to life," said Lise Buyer of Class V Group in Silicon Valley, which advises companies preparing for IPOs.

(Reporting by David Lawsky and Phil Wahba; Editing by Tiffany Wu and Richard Chang)