

High-profile successes highlight Ann Arbor's Arboretum Ventures as state's leading venture capital firm

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Robert Ramey Arboretum

Ventures Managing Director Tim Petersen and company founder Jan Garfinkle.

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Bolstered by a series of high-profile investments and a home-run local deal that yielded a 10-fold return, Ann Arbor-based Arboretum Ventures is emerging as the state's leading venture capital firm.

But founder Jan Garfinkle emphasizes that she expects to be much more than that.

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"Our goals and our aspirations are to be one of the best venture funds in the nation in medical devices and health care services," she said.

Arboretum, which made five investments in 2008 and reaped huge returns on a 2005 investment in Ann Arbor-based health care software firm HealthMedia, is poised to finish fundraising for its third investment fund.

Arboretum executives declined to comment on their fundraising activities due to SEC regulations.

But they are poised to play an increasingly influential role in the state's venture capital community - particularly after Ann Arbor-based \$100 million VC firm Ardesta announced this fall that it would no longer make any new investments.

In October Arboretum reaped at least 10 times its investment when pharmaceutical giant Johnson & Johnson acquired HealthMedia, Arboretum managing director Tim Petersen said. Arboretum also made a high-profile investment in Lipitor co-discoverer Roger Newton's startup Esperion Therapeutics in 2008.

Meanwhile, economic development group Detroit Renaissance's new Renaissance Venture Capital Fund has invested \$5 million in Arboretum, which invests in entrepreneurial health care and medical devices companies. It was the first investment for the Renaissance VC Fund.

In Arboretum's five years in operation, the Michigan companies it has funded have added about 300 employees. Arboretum has some \$90 million in capital under management.

Garfinkle and Petersen recently sat down with Ann Arbor Business Review reporter Nathan Bomey to discuss their investment strategy and their outlook for 2009.

Business Review: HealthMedia was a home run deal for you and others. When did you know it was a can't-miss investment?

Petersen: I had been familiar with the company from my days with the Wolverine Fund. I had known Ted Dacko since '99 or 2000, had been acquainted with Vic Strecher.

They needed a growth round of capital in 2005. And they invited three funds to consider investing.

The company wasn't a sure thing, but you could see a clear path to growth and profitability. Within a year it was pretty clear that we had made a good decision.

Garfinkle: They had incredible clinical trial data with a study that they had done with Kaiser Permanente.

What really pushed us over the edge with the investment was seeing such substantial clinical improvement with patients on their service.

Let's talk about Esperion. It's a slightly different strategy for your investment portfolio. Is this a one-time foray into biosciences. or do you expect it to be the first of many?

Garfinkle: I think for Fund II it will be the only one we'll make. Roger Newton is a tremendous CEO and obviously has an excellent track record - both with developing Lipitor and then the first Esperion.

We were thrilled to be able to back Roger, quite honestly. For Fund III, we haven't decided yet what we'll do with that.

Petersen: Anything in the health care space is in our purview. We've always articulated to both our investors and the world that we're most interested in devices and diagnostics and health care information companies.

But we always kept the option open to get into something like this.

Are you afraid expectations for Newton might be too high considering what happened the first time with Esperion?

Petersen: The first time around they went public and they didn't have a single product in the clinic. It was all animal work.

Will that happen again? That's not our expectation.

Garfinkle: But we do have high expectations that it will ultimately be very successful. We know Roger very well. He is incredibly thoughtful. He's a great visionary.

It may not turn out exactly the same, but I still have pretty high expectations that it will turn out very well. Roger, being the visionary that he is, he has put together a terrific team.

He has an excellent group of investors, and I think the combination of all of those lends to the possibility of being a great exit.

The public markets are down right now. But it's not even close to being ready for an exit. It's only a six-month-old investment.

Petersen: There are three other investors there from very large funds, so the company can just continue to progress for a number of years with the existing investor base. That's the way we looked at it.

Recently some health care organizations have been scaling back their growth. How does that impact your investment strategy?

Garfinkle: The wave of people that are going to need health care just because of being older is going to swamp the health care system. There will be volume growth as a consequence of that.

Right now it's a difficult time. There probably will be a slowdown.

But if you look at the big med-tech companies - which are the companies, like the J&Js, that will be the primary acquirers of our portfolio companies - they are holding their own pretty well. Their stocks are down a little bit, but they still have a lot of cash flow because they are getting paid by the insurance companies.

I think health care is somewhat insulated from the overall total recession that's going on, and everything will eventually bounce back once we right this ship.

Petersen: Short term everything's affected to some degree, health care less than most things. Longer term, nothing has changed in terms of lifestyle and demographics.

How conservative do you expect to be with your strategy in 2009?

Garfinkle: Our bar has always been extremely high for the companies that we invest in, and I would expect that to continue. What's different now honestly is that the pricing of buying into these companies is different.

The later-stage companies are having a more difficult time fundraising, so we are seeing some opportunities on the later-stage side that are pretty attractive from a pricing standpoint. ...

They're struggling to find funding more so than the early-stage companies, primarily because they need a lot more dollars and those dollars have dried up quite a bit.

What's your analysis of the state's commitment right now to venture capital, and are you concerned that with the state's economic difficulties, they'll scale back on it?

Petersen: The good news is that the Venture Michigan Fund and the 21st Century Investment Fund were completed, set up and capitalized two or three years ago, and they're approaching the end of the process of making those initial commitments.

The natural extension of your question is what happens next. Do they do this again?

I haven't thought a lot about that.

Garfinkle: I think it would be great if they would create Venture Michigan Fund and 21st Century (Investment) Fund II - primarily because we really need some more venture funds in Michigan. It is challenging to be a venture fund in Michigan.

We have had great success - knock on wood. But we'd really like to have additional co-investors in the state.

And personally, I think it's a shame - Ardesta announcing that they're not going to raise another fund. I would really like to see more venture investors, professional investors, in the state.

If the state needs to, if you will, juice it to make it happen by another series of Venture Michigan Funds or 21st Century (Investment) Funds, I think that would be a good thing to do.

2009 is going to be a really difficult year for the economy. How does the auto crisis threaten VC and Arboretum?

Garfinkle: I'm not sure the auto industry specifically impacts us. What it does do is send a negative aura about Michigan, which has been out there for several years now.

It can make it difficult for recruiting. I still think everyone views Michigan not in a favorable light because of what's going on with the automobile industry. ...

(But) we're feeling pretty good quite honestly about 2009 and not being too negatively impacted by the global economy.

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