Investing in Emerging Technology-Based Companies

AURORA FUNDS

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2003 Outlook

The past year was, as anticipated, a challenging one for the economy in general and venture capital firms in particular. Looking ahead, 2003 will continue to be a difficult environment for existing portfolio companies, especially when it comes to fundraising and exits. Capital markets are not expected to show any improvement until late 2003 or early 2004.

Jeff Clark, Aurora Funds Managing General Partner, summed up the situation quite simply: "We are living through uncertain times. Adding a war and fluctuating oil prices to an already roiling economy makes it hard to see exactly when the clouds over potential exits will lift."

As a result of this muddled environment, portfolio companies actually have very clear priorities.

They need to show investors that they are actively proceeding on a path to profitability and positive cashflow. They need to demonstrate that the milestones they have established are being met. In a nutshell, they need to make it absolutely clear to existing investors that substantial progress is being made toward financial goals.

As far as fundraising is concerned, Aurora Managing General Partner Scott Albert said, "...the emphasis has to be on raising money to 'get your company home.' When you raise this money, you have to focus on getting enough to finish what you started." Future expenditures should be considered, so that portfolio companies can attempt to raise all necessary funds at one time, and no additional money is needed. If additional rounds are needed, a substantial portion of the new round should be provided by the existing investors.

"Right now, the tumultuous economic conditions – combined with war efforts of unknown duration and a thinly traded stock market – make exits of any kind difficult," Albert explained, "let alone on terms that are advantageous for our portfolio companies." With a successful round of fundraising completed, companies will have the resources and the flexibility to wait out current market situations for favorable exit windows to open.

It should come as no surprise that with current conditions, "entrepreneurial tourists" have given up the hunt and returned to their day jobs. Nonetheless, the southeast is still witnessing strong deal flow.

"What we are seeing now are many strong deals coming from the tried-and-true players," said Clark. Experienced managers are working together to establish companies with smart business plans and targeted at promising niches.

According to Clark, there are some very exciting early stage life science opportunities coming out of work being done at area universities. Regado Biosciences, for example, is a portfolio company building on efforts originally begun at Duke University to create products for the multibillion dollar acute care medicine markets.

In the IT sphere, Aurora is setting its sites specifically on early stage opportunities put forth by known entities. "We are looking primarily at companies where we know the teams in charge," said Albert. "We've had – and are having – great success with this approach."

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Overall, Aurora will seek out management teams that are experienced and that have demonstrated the ability to achieve positive results. "These days," Albert added, "early stage efforts are only going to be successful if the people in charge understand both how their specific business works, and how the venture capital world operates."

Fundraising for Aurora's fourth fund, Aurora Ventures IV (AV IV) has continued apace; final close is expected in April, with a target size of $75 million. The most recent investments have been made in XActional, Inc., StrikeIron, Inc. and Metabolon, Inc.

Aurora anticipates closing on five to seven new deals a year, and are looking to grow companies out of revenue and profit, rather than by burning through investor capital. They are particularly interested in companies that require only a modest amount of capital – $10-15 million – to "get home."

This approach will allow AV IV to retain a greater ownership percentage of the portfolio company, while at the same time giving investors greater flexibility in evaluating exit alternatives.

AURORA COMPANIES
In The News

Unitive, Inc., the leading provider of wafer-level packaging solutions that make semiconductors smaller, faster and lighter – has been named North Carolina Electronics & Information Technologies Association (NCEITA) Private Company Of The Year.

NCEITA award winners are companies that demonstrate outstanding vision, creative innovation and global leadership. Unitive's proprietary Electroplated Wafer Level Packaging technology has been recognized as the benchmark standard with which others compare themselves on a global basis. Unitive partners with its customers to meet their product and worldwide manufacturing needs through innovative deployment of its technologies, resulting in quicker time-to-market and lower costs.

VetCentric, a prescription drug distribution company serving the veterinary marketplace, has secured $14.5 million in a Series B round of financing.

In addition to the Aurora Funds, Sherbrooke Capital, a new investor, provided $4 million for the round, co-leading the financing with Three Arch Capital, an existing shareholder. Other previous investors taking part were Asset Management, Staenberg Private Capital and Vantage Venture Partners. Proceeds from the round will be devoted to marketing of its products, as well as to establishing partnerships with national animal healthcare providers. The new funds will also go toward upgrades of systems and infrastructure. VetCentric provides veterinary-focused pharmacy services, including home delivery of prescription medications and therapeutic diets to pet owners on behalf of veterinarians.

TriVirix International, a full-service contract manufacturer of electronic medical equipment, announced that it secured a total of $25 million in private equity.

Aurora Funds seed funded the company in 1998 and has participated in each of the four rounds of venture financing that the company has received. New investors in this round included Grotech Capital Group, Morgan Stanley Venture Partners, MDS Capital, SunTrust Equity Partners, Trelys Venture Partners and MB Ventures. Repeat investors included Thompson Clive and partners, Frontier Capital, Enterprise Equity, Crescent Capital, Charlotte Angel Partners and Tri-State Investment Group. Richard West, TriVirix CEO, sees this as a perfect time to grow aggressively, while other companies are contracting. TriVirix, recently ranked ninth in the Triangle Fast 50, completed two acquisitions with the purchase of a medical electronics assembly plant and a printed circuit board assembly plant. The company plans to expand its geographic reach and service breadth with the new capital.

Gómez, Inc., the leading provider of Internet application performance measurement solutions, has acquired WebPerform Ltd, a privately held UK-based company.

WebPerform provides technology and services that trace, measure and correlate online customers' behavior with Internet site's operational and technical performance metrics. From this acquisition, Gómez – which operates a proprietary global Internet performance measurement network – emerges as the only vender able to monitor and benchmark all variables that influence online customer behavior. The acquisition also adds substantial presence in the UK market, where WebPerform has established channel partners and blue chip clients in the financial services and retail sectors. According to Gómez CEO Alex Stein, the integration of WebPerform into Gómez addresses a gap existing in the performance management space. By combining the two company's technologies and consulting capabilities, Gómez can now show clients the most comprehensive picture of the relationship between web site performance and the experience and behavior of their online customers worldwide.

Stemco Biomedical, Inc., a company engaged in the development of hematopoietic stem cell (HSC) identification products, announced it has secured a Series B round of financing for $9.8 million.

The Aurora Funds co-led the investment along with Intersouth Partners. Other investors in this second round of financing included Becton Dickinson Ventures, Trelys Venture Partners and Tall Oaks Capital Partners. The company launched its first product earlier this year and will enter clinical trials for another product later this year. The transplant market alone for the products being developed by STEMCO is estimated at more than $1 billion annually. There are no high-profile ethical concerns with the use of STEMCO's products since they use traditional and widely accepted sources of HSCs that are not derived from fetal or embryonic tissues.

Portfolio *Talk*

STRIKE IRON

StrikeIron Hits the Ground Running with Experienced Management Team

StrikeIron, one of the newest companies in Aurora's portfolio, provides a prime example of one of Aurora's guiding principles: focus on the key people involved, and the rest will fall into place.

"As a rule, we invest in early stage companies guided by entrepreneurs and thought leaders who have a clear, powerful vision of the future," according to Scott Albert, Aurora Managing General Partner. "And wherever possible, we work with people who have a proven track record in shepherding entrepreneurial dreams toward successful exit opportunities."

Albert added that a critical part of any business plan is the people who stand behind it. "These days, especially when we're looking at IT opportunities, that's where you have to start. You have to ask, 'What have they done? Do they know how to make things work in the real world?'"

In the case of StrikeIron, the answers were obvious. Included on the founding management team are well-known Triangle entrepreneurs Richard Holcomb, Robert Brauer and Robert Dale.

Holcomb helped launch Q+E Software, which was acquired by Intersolv in 1994. He was a founder of HAHT Commerce, a major e-commerce application provider, and served as its first CEO and Chairman. Holcomb is also a Venture Partner for The Aurora Funds.

Brauer co-founded startup DataFlux in 1996, with Holcomb as a member of the board, and Aurora Funds as an investor. DataFlux, a highly successful software company, was purchased by SAS in 2000.

Dale has more than 25 years of experience creating innovative enterprise software. He founded and served as CTO of KVLabs, a company that developed configuration management software for Microsoft-based networks, and co-founded and served as CTO for CI Technologies, which was acquired by Seagate Software in 1995.

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"This is an ideal fit," said Albert. "Aurora was able to get involved at a very early stage and work with an experienced management team – in fact, people who we've partnered with before – to build this from the ground up."

The new venture focuses on web services, a very promising and quickly spreading technology. The term web services covers a range of software that allows real-time application-to-application communication over the Internet. Some familiar existing implementations include instant messaging, traffic updates, in-game sports scores and stock tickers, which can be delivered to users' desktops or made available on hand-held or portable computers.

Brauer sees the real promise of web services in the business-to-business arena. "This technology will enable companies to communicate more quickly, clearly and efficiently with suppliers, customers and partners." It will also, he said, help to streamline internal communications between different legacy systems.

StrikeIron intends to stake out a position as an enterprise-class provider of products that will enable both developers and end-users to easily develop and deploy web services application architectures in the multi-vendor, multi-technology environment of large IT organizations.

The goal is to make it easier for businesses to do business, says Brauer. "We're not going to be selling technology for technology's sake. Our products are designed to let organizations control and enhance how they use web services to solve problems and add value."

StrikeIron plans to have beta versions of some of its utility software available in midsummer, along with a prototype of its tool for greatly simplifying the creation of an interface for deploying web services. Initial marketing materials should also be available at the same time.

Portfolio Spotlight

United Emergency Services, Inc.

Growing Revenue Through Targeted Acquisition Positions UES For Success

United Emergency Services (UES), a Durham-based physician and nurse staffing and contract management company, has taken several steps to continue to improve its position in the marketplace. Aurora seed funded UES in 1996, and has been actively involved as lead/co-lead investor in the company since its inception.

UES recently completed the acquisition of Alpharetta, GA-based TVL Healthcare, a provider of traveling nurse staffing services. The acquisition will enable UES to focus more attention on higher-margin nursing and ICU staffing services.

In addition, UES continues to build its baseline revenue stream by signing staffing contracts with new hospitals. To date, the company has 30 contracts in place, and continues to be profitable; it reported approximately $28 million in revenue in 2002.

These developments are designed to enable UES to meet several key growth objectives, including geographic expansion and enhanced service offerings, as well as the increased profitability that will come through economies of scale and diversification into other attractive areas within the medical staffing business.

"Obviously, we're very pleased about where things are headed," said UES Founder and CEO John Hemingway. "We've been able to enhance and expand our offerings, and put ourselves in a position to become more profitable."

With the acquisition of TVL, UES reinforced its commitment to strategic growth – a by-product of its mission to provide exceptional recruiting and staffing services to a limited number of hospitals in the southeast. "We are not looking to become the biggest provider overnight," Hemingway elaborated. "We are going to grow by paying attention to the details – taking care of our customers, taking care of our doctors and providing a return for our investors."

The two critical factors behind any successful emergency physicians service are effective recruiting and the individual physician's commitment to the community. Matching the right physician with the right community is the key to satisfying the hospital client in the short term, and to building, over time, a strong reputation within the physician community that he or she serves.

Jeff Clark, Aurora's Managing General Partner, said that UES has staked out a position for itself to allow those things to happen. "UES focuses on providing experienced and well trained physicians and nurses to under-served single hospital communities in urban and rural areas. In its geographic target, as many as 500 hospitals fit the client profile."

UES does not go into this market as the low-cost provider. Instead, the company positions itself for success in the bidding process by ensuring that the physician is paid about 85% of contract dollars. This permits UES to provide quality service that meets the needs of the hospital, the physician and the community. With this model, UES is able to hold the need for value-added services to a minimum.

Clark is optimistic about the future prospects for UES. "Clearly, a staffing firm's management experience in dealing with community hospitals and physicians is instrumental to its success. John's reputation in healthcare, particularly in the southeast, gives UES an excellent opportunity to establish itself as an effective and reliable provider of emergency services."

United Emergency Services, Inc.

HEADQUARTERS: DURHAM, NC

Management Team:

John Hemingway,
Chairman/Chief Executive Officer

Robb Cadwallader,
President

Kirk Doolittle,
Sr. Vice President – Operations

David Wellman,
MD, Chief Medical Officer

Karen Moss,
Vice President and Controller

Dawn Parry,
Vice President Marketing/Sales

Subha Tholudur,
Recruiting Manager

Aurora Updates Web Site

Visit our newly revised website for complete information on our portfolio, our investment philosophy and our staff.

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The Aurora Funds News is a quarterly publication of The Aurora Funds, Inc., a Research Triangle Park, NC-based venture capital partnership that invests in early stage life science and information companies in the southeastern U.S.

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