

Private Equity Analyst

Edison Venture Fund Leaves No Stone Unturned In Exit Quest

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When venture firms boast of exits, they're typically talking about acquisitions or IPOs. Edison Venture Fund took a different approach recently when it announced an 11-times return on its initial investment in CambridgeSoft Corp., achieved by selling its shares back to the company.

At a time when traditional exits are harder to achieve, the Lawrenceville, N.J., firm, which has been around since 1986, says it is working harder to generate liquidity for its limited partners. "Exits are considerably more difficult now than they were earlier in my career," said John Martinson, Edison Venture's founder and a managing partner. "We're much more proactive."

The firm is seeing longer times to exit even though it is a later-stage growth investor and does not back start-ups. It invests in technology companies that are cash-flow positive or close to it. Most have been in business for three to six years and have no prior institutional financing.

Share buybacks work when a company is generating plenty of cash and has a management team that wants to keep building the business, Martinson said. Once the domain of start-ups with skimpy revenue, even the Internet sector now has some highly profitable companies with significant cash flow that "can buy investors out at multiples we're trying to achieve," he said.

In the case of CambridgeSoft, a provider of research software for health-care and chemical companies, Edison looked to exit because it had backed the company from a 1998-vintage year fund that had reached the end of its life. The firm had put a total of \$5.1 million into the company in two secondary transactions, one in 2002, the other in 2006, mainly by buying shares from early investors. Edison sold all its shares to CambridgeSoft for about \$40 million, generating an eight-times return on its entire investment.

Edison has done several similar deals and expects to do more, but because relatively few companies will be able to execute them, Martinson said, "It's a supplemental theme for us; it's not going to be a primary strategy." The CambridgeSoft investment also illustrates the firm's willingness to buy stock from prior investors and company founders to boost its ownership stake.

The firm considers itself an expansion-stage or late-stage venture investor and its targets are relatively small companies. In recent years, when Edison first invested, companies averaged \$8.5 million in annual revenue, said Managing Partner Chris Sugden. It looks to grow them to at least \$40 million to \$60 million in annual revenue over five to seven years. Edison has three companies in its portfolio with more than \$100 million in revenue and another six with more than \$50 million.

Larger growth-equity firms are potential buyers of Edison companies that can sustain high-growth rates. "There's a gap but that gap is closing," Martinson said of pricing differences that historically have made such deals difficult.

Edison expects that initial public offerings will continue to account for about 10% of its exits - it has two companies in IPO registration, GAIN Capital Holdings Inc. and Tangoe Inc. - but strategic sales remain the main source of liquidity. Edison says it is working harder on these, with a person dedicated to mergers and acquisitions. "We're almost acting as a partial investment banker for ourselves," Martinson said. With the slower pace of IPOs and the surfeit of venture-backed companies, "we have to be out front hawking our wares."

Edison Venture Fund

The Firm

Edison Venture Fund is a later-stage investor that looks for technology companies along the Eastern seaboard from Massachusetts to Virginia. Based in Lawrenceville, N.J., it has six partners and offices in Needham, Mass.; New York; and McLean, Va. The firm's average investment is slightly less than \$7 million and typically looks to initially own at least 35% of each company.

The Fund

Edison Venture has held a second close on an undisclosed amount for its seventh fund, which has a target of \$300 million. Its prior fund closed in 2007 with \$258 million in commitments from limited partners such as BlackRock Inc., Colorado Public Employees' Retirement Association and HarbourVest Partners LLC.

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