Quantifying Due Diligence

The healthcare market is a microcosm of a various categories that experience different growth and investment interest over time. Over the past two years, various categories have experienced more investment interest than others.

According to McGuireWoods, the following categories have seen more investments in the past two years:

1. Healthcare IT, HER, and HUB services
2. Behavioral health
3. Ophthalmology and optometry
4. Physician practice models
5. Telemedicine, remote monitoring

The following categories have remained steady in investments over the past two years:

1. Medical devices
2. Urgent care
3. Dental practices
4. Ambulatory surgery centers
5. Dermatology
6. Specialty pharmacy

The one sector that has seen less investments is hospital systems. This seeming factoid has eventual major implications in the overall trend of healthcare. The investment trends portend the overall trends in healthcare. A decrease in hospital system investors with a growth in more decentralized, technology enabled solutions likely portends an eventual de-centralization of the healthcare system. More specifically, understanding the changing dynamics in supply chain management, healthcare procurement processes, and patient engagement can help investors identify high growth regions to invest in.

At a very high level, growth in healthcare is fueled by large trends such as aging populations, evolving regulations, advances in key technologies impacting consumer interfaces, and back-office functions and low interest rates. But more specifically, the economics of healthcare, as cited above, have an equally noteworthy influence on investment growth.

Successful investments should not only identify such macro-trends, but also evaluate the investment opportunity itself. Start-up companies live and die by funding, but the most successful start-up companies focus equally on operations and execution.

Approaching investments on a milestone basis allows the investor to quantify the successes of the company and determine the company's likelihood for future successes. This allows investors to see beyond the common refrain of regulatory risk and identify promising ventures. Since the identification of many well-defined ventures is usually desirable to increase the probability of executing profitable investments, the life science investor also needs to be particularly skilled in filtering down these various findings to the most promising prospects. The use of rapid

evaluation techniques is usually the preferred method to accomplish this filtering task. Risk mitigation in this phase of the life science process demands that investment screening be conducted as quantitatively as possible. However, tools to assist investors in quickly and efficiently filtering promising life sciences investment prospects are virtually absent.

The ideal model consists of a rapid initial evaluation followed by a more comprehensive, detailed evaluation. The initial evaluation should focus on more traditional metrics of start-up evaluation: market size, competitive analysis, etc. The subsequent detailed evaluation should build upon the traditional metrics in more detail but include equal analysis of the clinical fundamentals underlying the company's value proposition.

A weighted analysis that formats the answer choices in either a binomial 'yes or no', or Likert format allows multiple members within an investment group to efficiently share answer responses and compare multiple companies at one time. Standardization of the due diligence model begins by defining a structured approach to evaluating the company initially and subsequently with a more in-depth analysis. It also requires all members of an investment group to understand the analysis equally. Standardizing the responses from the company allows all prospective investors to gauge the investment likelihood of the company.

MD Angels has a robust model of due diligence that is based on quantifying the company evaluation from the initial evaluation to the final investment decision. The growth and success of our angel group is predicated on leveraging this model to make disciplined decisions.

Such a structured approach allows MD Angels to execute on investment decisions far more efficiently than most angel groups. Typically, angel groups operate in a more ad hoc, gut feel manner. Yet studies have shown that this approach is a principle cause of not investing and/or failed investments. Most investment decisions that fail upon execution are due to the following reasons:

1) Absence of standard operating procedures to quantitatively evaluate and compare life-science investment prospects
2) Unfamiliarity with market trends, regulatory barriers and technical development timelines in the healthcare sector
3) Insufficient resources required to evaluate each investment opportunity
4) Inaccurate estimations during valuation
5) Failure to efficiently compile accurate information regarding actual status of technical development, clinical validation and investment needs

Having a standardized investment model that emphasizes the deep clinical insight of our members as well as a diverse board of directors that can evaluate every aspect of a company in the life sciences space allows MD Angels to assess a wide array of deals and execute on investment decisions in an efficient manner. We pride ourselves on our domain expertise in the clinical realm and have extended the same level of discipline into our evaluation of healthcare start-ups.