

Fuelling growth in an equity-poor market

It starts with an idea. Given sufficient private capital, a life science company is born. When a credible concept is developed, the search for venture capital begins. After several rounds of financing, owners take the company public.

Unfortunately, there is a flaw in this formula for today's life science companies: the window for raising public equity markets is effectively shut. Companies that, not long ago, thought they would be able to raise capital through IPOs are being forced to cut spending. 'That could impede work crucial to growing the business to where it will be attractive for an acquisition or IPO once capital markets open up,' says Anthony Storino, managing director of GE Life Science and Technology Finance (LSTF). 'For many companies, there are better alternatives to extend the cash runway of a business.'

Extending operating windows

Given the dearth of equity, a young company needing equipment to continue its growth has two options: spend the equity it has or borrow. Consider a hypothetical company with \$3m in cash and operations burning \$100,000 a month. There is cash for 30 months, but what if equipment costing \$1m is needed? If purchased with cash, the operating window drops to 20 months. But if the equipment is financed, the cash window extends well beyond 20 months. 'In today's climate,' Storino contends, 'adding 6–12 or more months of cash to a balance sheet can be the difference between making a marketable discovery and running out of money.'

While equipment can be financed with a loan, a young company typically gains no financial benefit from owning equipment. Computers, laboratory and test equipment commonly used in life science companies become obsolete quickly. Further, the primary tax benefit of ownership – depreciation – is irrelevant to a company that is not earning profits yet.

Freedom and flexibility

With a lease, the lessor owns the equipment and can depreciate it for tax purposes. This lets the lessor reduce the borrowing rate it charges customers. Monthly payments are generally lower with a lease, freeing cash to use elsewhere in the business.

A lease also offers more options than a loan. 'What if you need to upgrade to better equipment?' asks Storino. 'That can be crucial to a research-driven business. A lease makes upgrading easier, without the burden of disposing of the old equipment. And if the

The economic climate may seem to militate against traditional business models for life science companies. Leasing provides a solution.

equipment proves useful, you can buy it for fair market value at lease-end. Leasing builds in some flexibility.'

Leasing also can provide a cash infusion. Storino explains: 'Say you bought equipment and now find yourself in a cash crunch. It's a common problem. An innovative lessor can buy your equipment and lease it back to you in a single transaction. You get cash, and your equipment stays in place. Importantly, this technique lets you raise cash without selling more of your business to outsiders.'

'GE knows the life science market and we know the equipment,' says Storino. 'We finance equipment a bank may not, simply because banks won't take a risk on equipment they don't understand. Banks often make business borrowers maintain a deposit account, too. That lets the bank lend you your own money. We don't require that.' Anything that might be in a life science facility, including the facility itself, can be leased or financed with a loan.

Storino advises prospective borrowers to choose a financial partner that can keep up with their needs when the business takes off. 'GE LSTF customers can start with us when they're small and stay with one financing company as they move through the business life cycle.'

With no clear signals that IPOs will soon return to favour, innovative financing can help life science companies create a longer runway to fuel continued growth and stay poised for opportunity when the capital starts flowing. ■

Company profile

GE Life Science and Technology Finance, a unit of GE Commercial Equipment Financing, which is a division of GE Commercial Finance, provides financial assistance to life science companies throughout the USA and Canada with a portfolio exceeding \$400m in served assets, representing over 275 customers. GE is a diversified services, technology and manufacturing company with operations worldwide.