In At The Deep End

The Tech Firms Which Have Lost The Most Money

By Nick Mulcahy

THE SOFTWARE AND general technology sector has benefited from huge private venture capital investment over the past five to seven years. However very few of the largest investees have turned profitable. Business Plus has extracted the latest filed accounts of more than 60 privately-owned software and technology companies trading in Dublin and ranked the top 25 according to their accumulated losses. The total losses for this Tech 25 is around €350m.

These investments represent a huge leap of faith by both indigenous and overseas venture capital firms. What the VCs hope for is a few home runs to pay for many more duds. Some of the firms in this Tech 25 listing will doubtless one day pay their backers a nice dividend. However it's possible that some firms will struggle to survive.

It's impossible to do a comprehensive scoresheet of whether VCs are ahead or behind on their overall investment in the Irish tech sector. Total investment in Ireland by VC, firms through 2004 amounted to €166m in 2004, (of which €113m came from foreign VCs) compared with €535m in 2003. That's according to PricewaterhouseCooopers, who monitor VC investment activity. Last year's fall was partially due to the absence of big MBOs in 2004 and total investment in 2004 was still above 2002 and 2001 levels.

Irish VCs invested €61m in 2004 almost entirely focused on startup and expansion stage companies; 88% of Irish investments were in technology companies with 56% going to computer related and communications companies. Funds raised in Ireland in 2004 for VC investment totalled €47m compared with €60m in 2003, a decrease of 22%. This is because none of the large Irish VCs did a fundraising in 2004.

While Dublin's technology sector can hardly be said to be thriving, one of the problems facing tech firms is that they are undercapitalised. Developing software, and trying to sell it to a global customer base, does not come cheap and it's notable from this survey that only a handful of companies have managed to secure share capital investment of over €10m. Joe Tynan of PwC's technology industry group notes: "The average amount invested into each company last year at only €510,000 is very small relative to the amounts invested in their European and US counterparts. This creates difficulties for Irish companies who compete in global market."

With so many loss-makers on their books, VCs have been pulling in their horns. According to PwC, VCs invested €28m in 48 startups in 2004 versus €33m in 106 startups in 2003. They invested €33m in 42 expansions in 2004 versus €47m in 86 similar companies in 2003. Desmond Fahey, chairman of the Irish Venture Capital Association, says that Irish VCs have capital to service investment needs over the coming 12 to 18 months, but will need to top up with "significant funding" in 2006.

Whether that funding will be forthcoming to the funds could depend on some of the companies in the Tech 25 being flipped for a profit. Divestments by Irish VCs reached record levels in 2004 at €191m. More than 90% of divestments were by way of trade sales, public offerings, debt repayment and sales to other investors. Write-offs accounted for €13m.

"While an increase in divestments is to be expected at this stage of the venture capital company's life cycle, 2004 was an exceptional year. This level of activity indicates that an exit market is developing, providing the essential disposal mechanisms to the venture capital industry," says Fahey.