

# Epidarex Capital: Will this fund be the poster child for early stage investment?



Sinclair Dunlop, Managing Partner, Epidarex Capital

**Epidarex is a specialist life science venture capital group that recently raised a new fund of £47.5 million dedicated to UK start ups and university spin outs. Backers include US drug giant Eli Lilly, the Universities of Edinburgh, Glasgow and Aberdeen, King's College London, the European Investment Fund, Scottish Enterprise and Strathclyde Pension fund.**

**Sinclair Dunlop is the fund's managing partner, and he talks to us of his ambition for the fund to become a catalyst for the sector, ultimately helping to bridge the early-stage funding gap while demonstrating a competitive rate of return can be made for investors in this sector.**

**B&M: Sinclair, I wondered if you can tell me a little bit more about the Epidarex fund itself, what is its history, who are its backers and what are its unique features?**

**Sinclair Dunlop:** It is a product of a model that we refined and built mainly on the east coast of the US, with an initial a focus on the mid-Atlantic region. The key driver of the model is to fill the equity funding gap between the seed and mid-stages of growing life science companies. .

We also believe in filling the gap in what we call, geographically, under-ventured regions. We've had

some success in the last 15 years in the mid-Atlantic of the US, looking for the richest scientific opportunities that are struggling to raise scalable venture capital. This challenge of accessing funding, particularly in the life sciences, is global.. And frankly outside of Massachusetts and California, it's almost as much of a challenge in the US as it is here.

About 3 years ago it became clear to us that probably the richest opportunity for life sciences and particularly under-ventured life sciences was in the UK, and especially in Scotland.

And that was when we started a conversation with some of the groups who became both our partners and our early investors, including the 3 top universities in Scotland: Edinburgh, Glasgow and Aberdeen. Scottish Enterprise, Strathclyde Pension Fund and the European Investment Fund also provided critical early support of our proposition.

Across the UK there are particularly rich opportunities to be found within the delta between a world class science base needing commercial translation and scalable risk capital to fund that translation. This gap in the UK probably offers more unrealised potential than in any other developed economy at the present time.

And so we saw a great opportunity. Many parties, including those coming from a public policy perspective, had already recognised this challenge, some on a glass half empty, others on a half full basis. We made the case, on a half full basis, to many of our early backers that the UK was in need of pots of scalable risk capital for the life sciences, and the plan

then became to raise an early-stage fund dedicated to the UK. And that was what we ultimately did. To the particular credit of those 3 initial universities, EIF, Strathclyde Pension Fund and Scottish Enterprise we pulled together the critical mass needed for our first close, and then we kept up momentum by attracting additional investors, from three leading UK family office investors and King's College London. And then we were very fortunate to bring in Eli Lilly & Company, North America's oldest blue chip pharmaceutical company that will bring an immense amount of resource and expertise to support some of our portfolio companies.

We've brought together a rich and diverse array of investors from the public and private sectors, including a leading financial institutional investors and a global 'blue chip' corporate.. And I think that's one of our greatest strengths. Because all of us are aligned in support for the sector and a shared determination to fully realise the potential of the UK life sciences sector. And that was the genesis of what has come about in the last 2 to 3 years.

**B&M: So if we look at the role of Epidarex in the sector as a whole, would you see it then as one of bridging the development gap - not just talking about very early stage but geographically as well?**

**Sinclair Dunlop:** Catalyst is a word that I like. It is of course unrealistic to think that we alone, with under 50 million pounds under management, can fill the gap but we hope to catalyse syndicates of co-investors alongside us to go some way to bridging the funding gap. So, over time, there should be a multiplier effect. And we're already seeing some encouraging signs by

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Our opportunity is to create a really exciting portfolio. We've got capital, a number of projects that we are looking at and projects we haven't seen yet. We're very much at the beginning of the life of the fund.

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being the local champion within the geography of the UK.

And regarding the geographic gap internationally, we like to think we're also beginning to add some value. Internationally we've been lucky to have interest from both Japanese and Korean investors who are increasingly keen to see what is going on across the sector in the UK.

We're therefore a potential conduit or the possible vehicle for those sorts of strategic dialogues. So I think there's a lot to be said for the UK as a good place to be building early stage biotech businesses. And overseas investors, whether they be global corporates or larger US venture funds are certainly looking around for investment or partnership opportunities in the UK. So there is both international bridging as well as internal, intra-UK bridging if you like. We are in the fortunate position to be able to bringing together principle investigators from different universities across the UK

to lead on the clinical trials of some of our current and future portfolio companies. We've also recruited some top executive talent into our first portfolio company here in Edinburgh.

I think if you can provide a critical mass of early-stage funding, at or above a certain threshold, that number probably being around 2 million sterling in seed or immediately post-seed funding, companies that were previously trying to scrape together a few hundred thousand, a lot begins to happen. There's a momentum threshold that is reached that also tends to attract management talent and other investors, critical for the providing follow-on funding, on the next step of the 'funding escalator'.

**B&M: If you could summarise the funds key goals, what would they be? And have you put any milestones in place to achieve those goals?**

**Sinclair Dunlop:** Obviously our number one priority

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which is also our fiduciary responsibility is to maximise the rate of return to our investors. And I don't say that flippantly because it's also strategically critical that we do that. Because, if we can't prove to institutional investors, the sources of hundreds of millions of pounds of capital needed into the sector, that you can make money and generate a competitive rate of return in this sector, in this geography, then we may as well all go home.

**B&M: If you look at that challenge then of delivering a competitive rate of return, what do you think is the biggest obstacle to doing that at the moment?**

**Sinclair Dunlop:** Timelines. Unlike any other sector it takes much longer to develop a product, to commercialise a product, to launch a product... it's incomparable to almost any other sector. You have to be patient. Life Science investing epitomises 'patient capital' if you like. No one should get involved in this sector thinking there's the probability of a quick win.

**B&M: So in terms of mitigating that, is it just a matter of educating investors of the timelines involved? Or how does one address that particular challenge?**

**Sinclair Dunlop:** I think yes, absolutely, for institutional investors that are not familiar or any investors, including angel investors or any type of individual investor, who is not familiar with the sector, it's important the sector does a good job of communicating just how lengthy development cycles can be, and just how impactful a single set back in a single trial can be in terms of investment return. The

same value inflection points also have potentially significant upside but it should 'eyes wide open' on all risk factors, from the start. Investors should know that companies that fail to meet those critical milestones, developmentally, will be closed down.

But you know, at the same time, a winner is a winner in this sector. Whilst it may be a long time in the making, if you hit the bull's eye you have the absolutely beautiful outcome of generating competitive investment returns whilst most likely also having a big social impact. That launch of a new drug or a medical device that offers a much more effective treatment, or even a cure potentially, for a large and unmet medical need is the goal that drives us all in this sector. And in that context, Epidarex spends a lot of time looking at 4 or 5 big disease areas, as well as some rarer and neglected diseases, where there is still a desperate need for more innovation and commercial success.

**B&M: How do you go about identifying the investment targets for the fund?**

**Sinclair Dunlop:** We spend a lot of time working closely with our university partners, as well as our contacts in industry, to source novel research and development that has significant commercial potential. We also spend a lot of time in that context with the key people, including founding scientists, as well as the management team that we'd back to take the innovation through the clinical and commercial development process. These teams are critical, because it is inevitably the case that whatever business plan Epidarex funds initially, it will not be the plan that gets a product to market or to exit. So it is around

the fundamental quality, complementary skills sets and overall flexibility of these teams where we spend the most amount of time, in terms of both our initial diligence and then our on-going post-investment support, which is critical.

Specifically, we like to get in very early with these Founders as well as in the recruitment of others so we can build teams, even prior to making our initial investment in some cases. We're also big believers in early and often lengthy dialogues with these individuals before we will write a cheque, before we become an investor. I think that's another unusual aspect of our sector, the entire review process followed by due diligence is much lengthier than in some other sectors. It would not be unusual for us to spend between 6 and 12 months completing an entire diligence process before we make an investment.

**B&M: I think what you mention about people is a very common thread that runs through all of the interviews we do at Biotech and Money. I guess what would help is if you're more specific. What exactly is it you look for in the people you're bringing together?**

**Sinclair Dunlop:** In terms of underlying traits, you need a degree of tenacity, self-confidence, intellectual rigour, commercial savviness, ideally with entrepreneurial experience – successful and unsuccessful. There's a lot to be said for a serial entrepreneur of whom we don't yet have enough in our sector in the UK. I'm potentially comfortable backing a CEO who might not have necessarily succeeded in his or her prior venture. Those individuals often have invaluable experience, as well as the courage to try

again.

**B&M: Sounds like you've basically got to be superman!**

**Sinclair Dunlop:** Pretty much! And then for academics and founding scientists, another key trait we look for is flexibility, particularly with regard to management roles going forward, and in some cases, an early acknowledgement that they're not going to be the CEO who ultimately takes this company all the way. . For example, it's prudent for all on a start-up's management team to acknowledge that at the right point in the company's growth it's going to be very helpful to bring in additional skills, in the form of a serial entrepreneur and/or seasoned industry veteran, who has previously developed drugs or devices all the way to commercial launch.

And the chemistry, pardon the pun, within teams, of complementary skills sets, is critical. And human attributes around the strength of personality are very relevant in these types of situations. Founders who acknowledge what they don't know, whilst excelling at what they do know, can be a gift to an investor in successfully pulling together entrepreneurial teams built for enduring success.

The teams that Epidarex funds are going to work together, practically 7 days per week for several years. And we're also going to support them 7 days a week. Whilst we're going to be on their boards we also aim to provide extensive additional support, almost on an as needed basis. . Some seem to think life as a VC is rather glamorous, where we just fly into board meetings and sit around and lay down the law. Our



experience at Epidarex is that nothing could be further from the truth. We're 'in the weeds', sleeves rolled up, getting stuck in if you like, often on a day to day basis. That's part of the job – as it should be. The 'nuts and bolts' of building very robust businesses is not that glamorous, it's often just hard work – and we're committed to it.

**B&M: And how would you assess the crop of potential targets at the moment? Are you satisfied?**

**Sinclair Dunlop:** I think it's very rich in the UK in terms of research and development across our sector. Aside from the obvious world class quality of our universities

and research institutions, we're particularly fortunate in the UK to have relatively sizeable sources of non-dilutive support which can be very helpful to our target investments. Epidarex's first investment, for example, in Edinburgh Molecular Imaging, a spin-out from the University of Edinburgh is developing highly novel fluorescent imaging reagents that detect harmful processes deep inside the human body, at the bedside, in real time and at molecular resolution. This very innovative translational research (spanning chemistry, biology, and medicine) from the University received prior funding from both Wellcome Trust and the Medical Research Council. We are also fortunate that the current UK government understands the importance of supporting early-stage innovation in our





sector. And in Scotland we are very fortunate to have a major economic development agency in Scottish Enterprise, along with its financing arm, The Scottish Investment Bank (SIB), that are very committed to supporting investor-led innovation in the sector. . SIB co-invested alongside Epidarex in our founding investment in Edinburgh Molecular Imaging.

You wouldn't necessarily see this level of support in most other EU markets and neither would you see it in many parts of the US. This support is helping enrich the flow of opportunities for Epidarex and other funds. That said, many of these opportunities still need some shaping, and still need some commercially-minded guidance as to their market

positioning and overall development strategy. It's our responsibility as investors to ensure our investees are not, initially, biting off more than they can chew and that, fundamentally, we're all agreed on a credible and therefore fundable business plan. Any investment Epidarex makes is heavily milestone-driven.

So in terms of opportunities, the quality of research and innovation in the lab and on the bench top is world class. The challenge is putting detailed, comprehensive and well-funded plans in place to deliver on the successful commercial translation of that innovation. Our next two investments, to be announced very shortly, will reflect this.

**B&M: The fund itself is quite young, only 1 year old. When do you think you will have a feel for if it will be successful?**

**Sinclair Dunlop:** We finished fund raising in April and we will be at least a 10 year partnership. I think we'll have a much better feel in how our portfolio in maybe 3 to 4 years now.

**B&M: And what would you say is the biggest opportunity that you have? What is the ultimate goal?**

**Sinclair Dunlop:** I think big picture we want to become the poster child for the idea that you can generate competitive rates of return in this sector. We have to be able to deliver on that, because there's so much more capital needed than Epidarex alone can provide. And again that's the point I was making earlier, we have to convince an institutional investor audience that this sector can't be ignored. With institutional capital, at scale, there is immense growth potential, over time, for the UK's Life Science sector. Even better, that growth comes with the opportunity to have a major social impact, in terms of significant improvements in patient outcomes.

What would be fantastic would be that if Epidarex could become the example that is cited by others in raising their funds. I think with the scale of the unmet funding need in the UK is such that there should be at least half a dozen funds like us kicking around the UK. There aren't that many right now and that's an opportunity. If others could hopefully follow our future success that would be ideal.

**B&M: It is an incredibly worthy aspirational goal to have. If you look at the road to get there, what do you see as the biggest challenge?**

**Sinclair Dunlop:** Another aspect of the access to institutional capital challenge, is for the UK to firmly establish that it has an active public market (i.e. flotation) option for some of our higher growth life science SME's. We've had a couple of successes in the last year that are encouraging, but we need to see more of that. If the shine comes off what's happening in the US markets, particularly with life science SME's listing on NASDAQ, that, obviously won't be helpful. If the City (of London) could further re-establish its coverage of and enthusiasm for equity investing in the sector that would be very helpful.

Ultimately, if we don't deliver competitive returns, and again if we can't prove that you can make money in this sector, that's going to be an obstacle to growth.

Another challenge is the need to ensure we're keeping enough industry R&D capacity, particularly with regard to our top 'med chem' talent, in the UK. There are currently too few opportunities for our top medical chemists in the UK. Some of this talent can be funded by the likes of Epidarex backing early industry spin-outs but more needs to be done.

Finally, and at the risk of stating the obvious, if the regulatory environment was to become more aggressive, that wouldn't be helpful.

**B&M: Are any of these trends you mentioned ones with which you are particularly concerned?**

**Sinclair Dunlop:** I think that there's always a regulatory concern. There's always a potentially high degree of regulatory risk present in our sector. And in some cases the regulatory burden seems unnecessarily high. There are also obvious issues with regard to public sector health systems, in terms of pricing pressures, approval of new drugs and NHS procurement. However, there seems to have been some recent improvement, particularly re the latter.

Another key task at a macroeconomic level is to make sure that the UK remains as tax competitive as possible. I would say the present government are actually aware of that. Capital is global, and flows away from any geography that is relatively punitive.

**B&M: Taking into consideration all those risks and uncertainties, and also the current realities we're in, would you say you're currently optimistic, pessimistic or indifferent for the UK life science industry?**

**Sinclair Dunlop:** I shouldn't be in VC if I'm not an optimist! I'm reasonably optimistic. I think the fact that big pharma is partnering early and bringing a lot of resources to the table is a very good development. Epidarex is very lucky to have our partnership with Eli Lilly in that context. I think the fact that public markets have opened up and that there are a few other VC's now managing to get their new Funds raised is very good news. We also have excitement now entering the public consciousness in areas such as cancer immunotherapy which is, rightly, another cause for optimism.

**B&M: One last question I'd like to ask. For the companies or targets that you're looking to work with, do you have any particular advice for these young companies or university spin outs that are looking to access venture capital?**

**Sinclair Dunlop:** Absolutely: come to us early, come to us before you're looking for money. Be honest with us, tell us the parts of your story you've worked out, and the parts of the story you haven't yet worked out. A "warts and all" approach generates confidence on our side of the table. I think the best we can do is give advice to entrepreneurs before they have necessarily set in stone the path that they're asking us to fund. We often find ourselves in the heart breaking situation where a company comes in and very proudly tells us what they've just spent a few hundred thousand pounds or a couple of million on doing and, in actual fact, it's not what we as investors or the market needs to see. In many cases we do find ourselves, even with a great piece of science at the core of the proposition, having to go back to the drawing board.

So I would always encourage entrepreneurs to come to us earlier rather than later. Come to us to discuss your proposition and potentially for advice before you need to ask for money. All of us at Epidarex have an immense amount of respect for the entrepreneurs we work with, and we're keen to help wherever possible. So entrepreneurs should of course try to sell us on their vision (and they need one!) but they should also tell us what they don't yet know. And that will actually engender trust and will most probably be the basis for a more functional relationship if Epidarex does ultimately invest. ■