Optics chips are tested at the Albuquerque manufacturing facility for Skorplos Technologies, a homegrown company that has grown its business through venture investment.

PRIMING THE PUMP FOR NM STARTUPS

State Investment Council programs could spur new wave of venture capital for emerging tech-transfer businesses
New Mexico is still mired in muck from the recession, but better times may be coming for local entrepreneurs looking to start new businesses.

About $40 million in new venture capital could soon be flowing into startups across the state now that the State Investment Council’s new Catalyst Fund has begun doling out money for local venture funds that want to pump up budding New Mexico companies. The Catalyst Fund, managed by Sun Mountain Capital in Santa Fe, approved the first $4.65 million in early May for three investment entities to back some of the wave of new businesses emerging from the state’s incubator and accelerator programs looking to take new products and services to market.

Those investments will provide a bridge for struggling startups to traverse the infamous early-stage financial ravine known as the “valley of death,” where emerging companies need a small amount of capital to further develop and prove their technologies before larger, institutional investors are willing to back them.

That, in turn, could attract a lot more interest from deep-pocketed, out-of-state investors to commit more money to help grow those firms into viable companies, potentially spurring a new cycle of venture investment here that New Mexico hasn’t seen since the Great Recession. That upward investment spiral, where startups can find larger rounds of capital as they grow and succeed, is a critical part of the entrepreneurial ecosystem that the SIC, state officials, and venture investors hope to catalyze through the new Catalyst Fund.

Economic Development Secretary Matt Geisel calls it another key instrument in the state’s tool box to spur economic activity, alongside Local Economic Development Act funds, employee training assistance for businesses and tax breaks.

“It gives us a new tool, and a unique one,” Geisel said. “It helps put more capital on the street to support new startups that transfer technology from our research universities and national labs to drive the commercial economy.”

Economic Development worked closely with the SIC and state and local officials to build the $20 million Catalyst Fund, which includes $10 million from the SIC-managed Severance Tax Permanent Fund, plus $5 million from the U.S. Treasury, and $5 million from private investors. Local funds receiving investments must match the Catalyst money dollar for dollar, potentially generating $40 million or more in capital available for local startups.

The Catalyst money will be channeled into eight to 10 local funds, which will then invest in 50 or more startups around the state.

As the money gets deployed and new companies advance toward market, New Mexico could capture a lot more of the immense amounts of venture capital now concentrated in places like the Silicon Valley, especially given the compelling, cutting-edge technology that local startups are pulling out of the state’s research institutions, said Julia Wise, manager of Economic Development’s Office of Science and Technology.

“It primes the pump for follow-on investment,” Wise said. “We have killer innovation here that can lure more capital away from traditional places like the East and West Coasts or Houston. We’re not trying to fill the capital gap, but strategically deploy our investment to attract more capital from elsewhere.”

Post-recession recovery

New Mexico had successfully attracted a lot of out-of-state venture capital before the recession through the SIC’s private equity program, which allows the council to commit up to 9 percent of the Severance Tax Permanent Fund to venture firms that invest in local companies. That includes a Co-Investment
Fund managed by Sun Mountain Capital for direct SIC investments in businesses.

Under the program, about 15 venture firms became active in the state, driving venture investment here to record highs of about $120 million per year in 2007 and 2008. But that plummeted when the recession hit, dropping to just $22 million in 2009 and then continuing at an annual average of about $37 million from 2010-2015, according to the New Mexico Venture Capital Association.

In part, that’s because the SIC ceased investing in local venture funds for about three years after the recession, and venture firms active here dwindled to only about half a dozen. Most of those remaining firms have concentrated only on follow-on investments in companies they had already committed to, rather than put more seed and early-stage funds into new startups.

Meanwhile, the venture industry nationally has flourished since the recession ended, reaching $79 billion in 2015, an 11-year record, and $69 billion last year, according to the National Venture Capital Association.

The lion’s share is concentrated in traditional bastions like California and the Northeast. But surrounding states have also managed to capture far more in new venture capital in recent years than New Mexico, which only netted $3.5 million in 2016, according to the national association. More than half of that was follow-on investments in existing companies, not money for new companies.

In contrast, Colorado captured $912 million last year, Arizona $297 million, Nevada $168 million and Utah $1.17 billion.

Out-of-state financiers

In 2013, the SIC did reauthorize new investments in venture firms doing business in New Mexico, leading to commitments to four funds since then. But until recently, many well-known national venture firms passed on the program, in part because previous rules mandated that they open a local office here, said Sun Mountain managing partner Brian Birk.

The state changed that requirement last year, now allowing venture firms with SIC money to operate from elsewhere and visit the state to scout for investments. As a result, a lot more firms have expressed interest, with 28 funds vetted by Sun Mountain last year for potential SIC commitments.

“That change resulted in a very full pipeline with interest from lots of high-quality financiers,” Birk said. “We’ve narrowed that down to three new funds, which are now in advanced stages for approval.”

With the Catalyst Fund now pumping money into local startups that may attract out-of-state financing, plus more SIC-backed venture firms ready to deploy money here, a new day may be dawning.

“I believe the situation will change dramatically in the years to come,” Birk said.

Local venture investors agree.

David Blivin, managing director of Cottonwood Technology Funds — which received a $2.5 million Catalyst Fund commitment this month — said the national pool of venture capital has grown significantly in recent years, and corporate-venture funding is also climbing. But New Mexico must seed a lot more local technology startups with early stage capital to grab the attention of national investors.

“We have really good, hard-science innovation here, and that’s a major strength for New Mexico,” Blivin said. “But we have to get it out of the labs and through proof of concept before investors take a serious look.”

Cottonwood has already invested in about half a dozen local startups in recent years, including Skorpios Technologies and TriLumina Corp., which are developing new breakthrough innovation in optics chips for high-speed data transfer and sensing applications.

The Catalyst Fund also awarded $800,000 to New Mexico State University’s Arrowhead Innovation Fund, and $1.35 million to Tramway Venture Partners, a new group focused on the life sciences. Both recipients expect to begin making startup investments this year.

That could be as soon as this summer for Arrowhead, which will invest in technologies either developed at NMSU or created by faculty, students and alumni. The Arrowhead Center, which manages all of the university’s technology transfer programs, has helped dozens of startups take their first steps to market in recent years. But only a few have achieved significant venture backing to date, such as the New Mexico Shrimp Co. in Las Cruces, which created technology to growing all-natural, saltwater shrimp in indoor tanks.

“The Catalyst Fund is critically important,” said Tramway Venture Director Waneta Tuttle. “It will greatly multiply the number of businesses launched in New Mexico. There’s no lack of opportunities here, but we need that seed and early-stage capital to get companies going.”
### VENTURE INVESTMENT IN NEW MEXICO AND SURROUNDING STATES IN 2016

<table>
<thead>
<tr>
<th>State</th>
<th>Number of Firms Funded</th>
<th>Total Investment</th>
</tr>
</thead>
<tbody>
<tr>
<td>California</td>
<td>2,658</td>
<td>$38 Billion</td>
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<tr>
<td>Texas</td>
<td>439</td>
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<td>Nevada</td>
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<tr>
<td>New Mexico</td>
<td>12</td>
<td>$31.5 million</td>
</tr>
</tbody>
</table>

Source: National Venture Capital Association

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Tracey Carrillo works at an indoor shrimp-growing plant in Mesquite, near Las Cruces, run by the New Mexico Shrimp Co., a venture-backed startup created with help from New Mexico State University’s Arrowhead Center.

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Lavu Inc. in Downtown Albuquerque won a $15 million investment last year from the Washington, D.C.-based venture firm Aldrich Capital Partners.

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