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Green Tinge Is Attracting Seed Money To Ventures

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SAN FRANCISCO, June 21 - Ira Ehrenpreis may be a kind of prophet advocating investments in alternative energy companies, but don't accuse him of being noble.

In recent months Mr. Ehrenpreis, a venture capitalist at Technology Partners in Palo Alto, Calif., has been asked any number of times to speak to audiences about "clean tech," a term that encompasses such things as solar energy, water purification systems and alternative automotive fuels.

He begins and ends every speech the same way: with a slide that stresses that to the extent his motivations are tinged green, it has to do with the color of money.

In Silicon Valley these days, more venture capitalists are following Mr. Ehrenpreis's lead. They are driven in part by the high price of oil, which hovered around \$59 a barrel on Tuesday, and the vast unmet demand for electricity in China and India.

"The reason we're allocating dollars to this sector is we think we can deliver attractive returns," said Mr. Ehrenpreis, who also serves as co-chairman of the advisory board of the Cleantech Venture Network. "It's not because we want to do great things for the environment or great things for the world," though he adds that that is a "great byproduct."

That message is resonating with venture capitalists and individual investors in the Valley, where growing rich through doing good is considered the ideal.

Top venture firms on Sand Hill Road in Menlo Park, Calif., are beginning to show serious interest in the alternative energy sector, though that typically means venturing outside their core expertise. They hope to capitalize on the growing worldwide demand for energy at a time of rising energy costs, and they see potential for huge profits in technology that can address challenges like climate change and dwindling natural resources.

"This is an area where we've been seeing a lot of quiet investing going on," said Mark G. Heesen, president of the National Venture Capital Association. "People are saying so far it's more talk than action, but I think there's been a lot of sub rosa action."

This month two of the area's top firms, Kleiner, Perkins, Caufield & Byers and Mohr Davidow Ventures, made large investments in solar energy companies. One, Miasolé, based in San Jose, raised \$16 million in a fund-raising round led by Kleiner Perkins. The other, Nanosolar of Palo Alto, raised \$20 million from investors led by Mohr Davidow.

On Tuesday, Energy Innovations, a company building advanced solar panels that use mirrors to track the sun and capture energy on storage cells, announced that it raised \$16.5 million in venture capital in a round also led by Mohr Davidow.

Energy Innovations, based in Pasadena, Calif., was founded five years ago by Bill Gross, a pioneer of Internet advertising in the mid-1990's. Mr. Gross gained fame in the dot-com era when the company he founded, Idealab, a privately held "incubator" of Internet start-ups, burned through \$800 million in eight months.

"I've had four years of conversations with V.C.'s on both coasts," said Andrew Beebe, president of Energy Innovations, "and I think we've seen a real change in terms of interest level and an understanding of this area."

He said that in recent months he had spoken with roughly a dozen venture capitalists, and half of them proved willing to talk deal terms.

The field is "starting to get big and grow rapidly," said Sunil Paul, a founder of Brightmail, an antispam company that was acquired by Symantec last June for \$370 million. Mr. Paul, an active investor in start-ups, has used his personal fortune to help finance three alternative energy companies. He was an early investor in Nanosolar, along with Sergey Brin and Larry Page, the founders of Google.

In February, more than 100 venture capitalists attended a conference on clean technologies in Palm Springs, sponsored by Clean Edge Inc., a consulting group based in Oakland, Calif. And it is a poorly kept secret within venture circles that at least two venture firms are trying to raise money for new funds that will focus exclusively on energy investments.

This attention by some of the Valley's highest-profile investors heartens Nancy C. Floyd, a founder partner of Nth Power, a San Francisco-based venture firm that specializes in clean-tech investments. It took Ms. Floyd and her partner more than three years to raise their first fund, a relatively modest \$63 million, which they started investing in 1997. Back then, Ms. Floyd said, it was very difficult to find a venture firm willing to invest with her firm on a deal, as venture capitalists tend to do on deals larger than a few million dollars.

"Energy had always had a very small core audience among venture capitalists," Ms. Floyd said. "It's only the last six months to a year we're seeing some of the generalist firms form teams around this and write checks in this area."

Interest from a broad array of companies, she believes, will help the entire sector. For one thing, big companies with expertise in, say, networking design or nanotechnology could provide invaluable expertise if they work with the right energy start-up.

Still, clean energy's share of the total venture pool remains tiny, according to data provided by Ms. Floyd's firm and Clean Edge, though it has doubled over the last four years. Mr. Paul, for one, noted that clean tech might need a success like a Yahoo or a Netscape "before every venture firm decides they need to be in this sector."

Clean tech represented a 1.2 percent share of the total dollar amount of venture capital invested in 2000. In 2004, the \$520 million that venture capitalists invested accounted for a 2.6 percent share of the overall venture pie.

"We're in a situation where we still have more deals than capital," Ms. Floyd said.

Mr. Ehrenpreis and Technology Partners, considered trailblazers in clean tech, began to focus more closely on these start-ups starting about five years ago. One reason was their reluctance to follow the rest of the venture capital industry, which at the time was shoveling tens of billions of dollars into dot-coms and telecommunications companies. A second was what they saw as the underfinancing of innovation in energy, given the potential markets.

"When you're talking about energy, when you're talking about water, you're talking about the largest markets in the world," Mr. Ehrenpreis said. His firm now devotes roughly half its resources to alternative energy start-ups. The rest is being invested in life sciences companies.

Similarly, Erik Straser, a partner at Mohr Davidow, spotted the great size of those potential markets and over the last three years decided to devote a large share of his time to exploring the clean-tech field. In addition to investing in Nanosolar and Energy Innovations, he and his partners have put money into a start-up that is using fuel-cell technologies to develop a portable, self-sustaining power plant.

"You look at all the development that's going on in China and India right now, and you realize that two-fifths of the world's population is going through the kind of industrialization that one-fifth the world's population experienced in the 20th century," Mr. Straser said. "The size of the opportunity here is immeasurable."

He pointed to Energy Innovations as an example of a company with a huge potential market. "If they can execute on their vision, they'll be a cash register stuck on open," Mr. Straser said.

Not every venture capitalist, though, is convinced that the energy sector is thick with companies with huge money-making potential.

Vinod Khosla, the prominent Kleiner Perkins partner, is bullish on the clean-tech field -- so much so that he stepped down as a full partner at Kleiner last year in part to devote more time to investing his own money in alternative energy companies. While he has already made four such investments over the last four years, he also doubts that very many clean-tech firms have huge payout potential.

"I have the sense that there are a lot more niche-sized start-ups out there than big ones," Mr. Khosla said, "but some great opportunities do exist."

While the federal government has scaled back investment in clean technologies, states are playing an increasingly important role, said Ron Pernick, co-founder of Clean Edge, the consulting group. Nearly 20 states have set goals for the percentage of energy supply that must come from clean sources, Mr. Pernick said, and some states, including California and Connecticut, are setting aside money to be invested in promising alternative energy companies.

Not since the days of the Carter administration, when the federal government was more involved, have venture capitalists been this excited about alternative energy, said Mr. Heesen of the venture capital association. And that time, he said, it "proved to be disastrous."

Today's landscape is radically different from that of the late 1970's, of course. Years of experimentation in fuel cells and solar energy as well as breakthroughs in other fields, from nanotechnology to semiconductors, have been great boons to innovation in clean tech.

But on the other hand, many firms just venturing into this field have no more experience today than they did 30 years ago.

Photo: Bill Gross, left, founder of Energy Innovations, and its president, Andrew Beebe, are reflected in the mirrors of one of its solar panel products. (Photo by Jamie Rector for The New York Times)(pg. C5)