

Venture capitalists warm to investing in alternative energy

With oil prices surging and increased talk of global warming, venture capitalists are straying from their traditional focus on computer technology and biotechnology to put increasing sums into alternative-energy companies.

Venture activity is way up in the past six months, with more energy companies presenting business plans to investors and more high-priced deals being done. Over the summer, four solar-energy companies attracted a stunning \$60 million in a round of high-priced financings that generated the first whispers an investment bubble may be forming.

For venture capitalists, "it's a very nascent market," says Warren Weiss, general partner at Foundation Capital. "It almost reminds you of looking at the Internet market 10 years before (browser pioneer) Netscape" unleashed the dot-com gold rush, he says.

Weiss says that in the past 18 months his firm has made three energy investments in an attempt to identify where advances in technology -- cheap, powerful chips, more capable software and broadband communications -- will have an impact on the energy business.

"You couldn't do it 10 years ago," he says. "We think the market is ready."

Weiss is not the only one to decide the time is right. Many white-shoe venture firms have named energy specialists and written funding checks, including Kleiner Perkins Caufield & Byers and Mohr Davidow Ventures, which became one of the year's more active firms with its first three investments.

"We see a great market opportunity," says Erik Straser, general partner at Mohr Davidow, who studied the business for almost three years before getting involved. "There's lots of innovation."

Two of the firm's startups -- Energy Innovations Inc. of Pasadena, Calif., and Nonosolar Inc. of Palo Alto -- make solar cells while the third, Jadoo Power Systems Inc. of Folsom, Calif., makes fuel cells.

According to a recent survey, venture investments in alternative-energy companies jumped this year, although they remain a small slice of the overall business. Venture capitalists put \$139.5 million into solar, wind and geothermal energy companies through the second quarter of the year, already surpassing the \$95 million they spent in all of 2004, according to the National Venture Capital Association, Thomson Financial and PricewaterhouseCoopers.

Other groups monitoring the market see a similar rise in spending, if not as steep. Nth Power, a venture firm focused on energy, calculates venture firms and venture arms of corporations put \$690 million in emerging technology companies in 2004 and already close to \$533 million through September of this year. The numbers are higher because Nth Power includes investments not only energy producers but technology companies -- such as software firms -- that make products for the energy business.

"There's no doubt we are seeing quite a bit more activity," says Tim Woodward, managing director at Nth Power.

Cleantech Venture Network LLC also is seeing more funding take place. The research organization says \$189.4 million went into energy-related venture deals in the second quarter, up 42 percent from the first quarter. The company also uses a broad definition of an energy company that includes startups making energy-generating equipment, as well as batteries and products to improve energy efficiency, such as low-power lighting.

More money is on the way. Between 80 and 100 funds are out raising new money to invest in "cleantech," a term that includes energy companies and environmental businesses with transportation, water-purification and air-improvement projects, says Nicholas Parker, chairman of Cleantech.

The recent surge in energy investing isn't hard to understand. With oil prices around \$65 a barrel, alternative-energy sources become more competitive, especially with subsidies in many countries and new subsidies in the United States.

Venture capitalists also see opportunities in the fragile power-transmission grid. "The first shock to the system was the Northeast blackout" of 2003, says Woodward. Yet, even as the health of the Earth may be under assault from global warming, the potential demand for power remains enormous.

Venture capitalists say there are good and bad sides to the surge in energy investing. On one hand, "it's easier to put together investment syndicates than it used to be," says Peter Edwards, a partner at Altira Group LLC, an energy VC. On the other, "I would say there is more competition," he says.

So far, the valuations being paid in energy deals remain reasonable. But prices are creeping higher, and some VCs say the danger of a bubble is real. Nanosolar, Miasole of San Jose, Calif., Energy Innovations and HeliVolt Corp. of Austin, Texas, closed on a total of \$60 million in a few short weeks, leading some to suggest the category is overheated.

"I think the (solar) market will absolutely continue to grow," says Woodward. But "not every one of those companies will succeed."