

H&Q LIFE SCIENCES INVESTORS  
Form N-CSR  
December 01, 2009

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

**FORM N-CSR**

**CERTIFIED SHAREHOLDER REPORT OF REGISTERED  
MANAGEMENT INVESTMENT COMPANIES**

Investment Company Act file number 811-06565

H&Q Life Sciences Investors  
(Exact name of registrant as specified in charter)

2 Liberty Square, 9th Floor, Boston, MA  
(Address of principal executive offices)

02109  
(Zip code)

2 Liberty Square, 9th Floor, Boston, MA 02109  
(Name and address of agent for service)

Registrant's telephone number, including area code: 617-772-8500

Date of fiscal year end: September 30

Date of reporting period: October 1, 2008 to September 30, 2009

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**ITEM 1. REPORTS TO STOCKHOLDERS.**

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**H&Q LIFE SCIENCES INVESTORS**

***Annual Report***

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**T**o our Shareholders:

On September 30, 2009, the net asset value (NAV) per share of the Fund was \$11.32. During the twelve month period ended September 30, 2009, total return at NAV of the Fund was -6.67%, with distributions reinvested. During the most recent six month period ended September 30, 2009, total return at NAV of the Fund was 14.62%, with distributions reinvested. The total investment return at market with distributions reinvested was -5.56% during the twelve month period ended September 30, 2009 and 21.14% during the six month period ended September 30, 2009. This reflects a substantial recovery in the market and a modest reduction of the discount. Comparisons to relevant indices are listed below.

<b>Investment Returns</b>	<b>Six Months Ended 9/30/09</b>	<b>Fiscal Year Ended 9/30/09</b>
Investment Return at Market	+21.14%	-5.56%
Net Asset Value	+14.62%	-6.67%
NASDAQ Biotech Index (NBI)	+22.96%	+0.42%
S&P 500 Index	+34.02%	-6.88%

**Portfolio Highlights**

This has been a difficult period for the Fund and for the markets. The fiscal year began as dramatic downward moves in both the S&P 500 and NBI indices were underway. As you are doubtless aware, there was tremendous upheaval in the markets in the fall of 2008. During this period the Fund acted defensively, increasing cash (and in so doing realizing losses) during a period in which the markets were falling. At midyear, we reported that on a NAV basis the Fund had performed comparably to the NBI and both the Fund and the NBI had significantly outperformed the broader S&P 500 Index. As we also reported in the semiannual report to shareholders, the Fund continued reducing exposure to the smallest healthcare related companies. In our experience, such companies tend to be early stage unprofitable companies highly reliant on the markets to raise operating capital. While a few such companies have done well over time and the small cap group occasionally outperformed as a whole, in general these companies have underperformed their larger counterparts over a relatively long period of time. The Fund ended March 2009 underweight small cap stocks. Unfortunately, for most of the six month period ended September 30, 2009 small cap stocks, in both the

biotech space as well as in the broader market, have outperformed larger cap stocks. Specifically, NBI companies with market capitalization of \$500M or less experienced weighted average stock price increases of ~76% in this period compared with an increase of just ~15% for larger companies. A similar outperformance of smaller companies occurred in the broader market as well. In healthcare, small cap outperformance has been attributed to a number of factors, including a positive generalized impression of the potential for mergers and acquisitions. In any event, being underweight this group of stocks hurt the performance of the Fund in the last six months of the fiscal year.

While performance of the Fund has suffered in this period, we are not abandoning our basic premise. We believe that the companies that will do best are those with quality marketed products that make a difference in the lives of patients and with solid management that has the ability to bring products with novel differentiated profiles to market. We also favor companies that can fund operations through partnerships or cash flow rather than through highly dilutive capital raises. The Fund does selectively own stocks of some companies that are farther away from commercialization which we believe can contribute to upside performance, particularly in the venture portfolio. However, we prefer companies with products in development. Typically, there is sufficient data associated with such products that we can use the medical, scientific and business experience of our excellent analytical staff to make assessments that we anticipate will produce solid returns for our shareholders.

A number of events in the healthcare and biotech sector have occurred involving both the general market and specific companies. The most important factor during the report period has been the unfolding of the national debate on healthcare reform, the goal of which is universal health insurance coverage for all Americans, a laudable and extremely ambitious goal. The debate has appeared to distill down to how to balance a wish to provide coverage and the uncertainty about how such an entitlement will be paid for. There are likely to be many winners and losers when, and if, a comprehensive law is enacted, but it is simply too soon to tell what groups will benefit most, or least. Generally speaking, healthcare stocks have underperformed the market since the Administration unveiled its reform ideas in late February after having outperformed the broad market in the latter part of 2008 and early part of 2009. We expect that such underperformance could continue until there is clarity about the outcome.

If there is one thing we have learned to count on, it is that stock prices are often weak whenever there is uncertainty, and there has been considerable uncertainty about what healthcare reform will look like and whether we will ultimately get comprehensive healthcare reform. Because of uncertainties, it is our impression that

generalist investors have avoided healthcare stocks during the last six months or so, preferring to wait to see what is or is not passed into law. Once the outcome is more certain, which we expect at or around the end of 2009, we expect that many investors will increase allocations into the healthcare sector. We would anticipate this to ultimately be good for the healthcare sector. Within healthcare subsectors, we believe that individual stocks are subject to dynamic assessments by investors about what their probability of success will be under any new healthcare legislation. As an example, consider the managed care sector, as exemplified by United Healthcare, Aetna and Wellpoint. This group sold off significantly after the initial February 2009 announcement by the Administration under the assumption that the sector's business would be harmed by governmental control or by a "public" healthcare insurance option. However, in the intervening months, this group rallied strongly. In part this upward move has been market related. However, there is also mounting speculation that healthcare reform may be good for the group as business (or at least pricing) lost to government control can be balanced by increasing volume provided by more people under coverage. This group continues to be affected by the fate of the public option. We believe that the best way to invest in the current dynamic environment is to identify and own companies with strong fundamentals that provide differentiated products addressing unmet medical needs.

In addition to these macro factors, a number of company-specific events have also shaped the healthcare and biotech market in the fiscal year. In addition to those noted in the semiannual report, we note positive reports or product approvals from such companies as Human Genome Sciences (BLISS-52), United Therapeutics (Adcirca and Tyvaso), Amgen (Denosumab), Dendreon (Provenge), Celgene (Revlimid), Abbott (Xience), Onyx (Nexavar) and Cephalon (Treanda). Similarly, there have been negative events at such companies as Sequenom (SecureDX), Osiris (Prochymal) and Genzyme (general manufacturing issues). We also note that mergers and acquisitions appeared to play a role in the current period. Acquisitions involving such companies as Medarex, Cougar, CV Therapeutics, P&G Pharma and Stiefel Labs appeared to catalyze a general interest in relatively small biotech companies. Overall we see the last six months in particular as providing a net positive set of news for the sector.

As noted in our semiannual report, the Fund realized some losses during the six month period ended March 31, 2009. This caused the Fund's distributions in early 2009 to be projected to be a return of capital. Given the uncertainty of the markets and the possibility of a negative tax consequence for shareholders in 2010, in August 2009 the Trustees of the Fund elected to suspend the Fund's distribution plan until further notice. We can report that, by the end of the 2009

fiscal year, sufficient gains had been realized by the Fund that, as reported herein, the Fund ended the fiscal year with net realized gains. We expect that the fact that the Fund ended the fiscal year without net realized losses will be a positive factor in the Trustees' evaluation of whether to reinstate the distribution plan. Many other factors will of course be considered and there is no certainty that the distribution plan will be reinstated.

After the suspension of the distribution plan there was a noticeable widening of the Fund's discount to its NAV. The discount has narrowed somewhat in the interim but remains on average higher than it has been over the last several years. In part, in an attempt to narrow the discount further, the Trustees have approved and the Fund has announced a share repurchase program. We are hopeful that this will have a beneficial effect on the Fund's discount.

#### **Investment Changes**

During the twelve month period ended September 30, 2009, within the public portfolio, the Fund established positions in several companies including Cephalon, Inc., Illumina, Inc., Cubist Pharmaceuticals, Inc., Perrigo Company and Warner Chilcott plc. During the same twelve month period, the Fund exited its position in several companies including Baxter International Inc., Genentech, Inc., through an acquisition, ICON plc, Masimo Corporation and Thermo Fisher Scientific Inc.

During the same twelve month period, within the venture portfolio, the Fund established positions in Interlace Medical, Inc. and Palyon Medical Corporation. The Fund made follow on investments in Concentric Medical, Inc., Magellan Biosciences, Inc., TargeGen, Inc. and Xoft, Inc. The Fund exited its position in Cytologix, Inc. and wrote off its investments in EPR, Inc. and Syntiro Healthcare Services.

As always, if you have questions, please feel free to call us at (617) 772-8500.

Daniel R. Omstead  
President

## H&Q LIFE SCIENCES INVESTORS

### LARGEST HOLDINGS BY ISSUER

As of September 30, 2009

<b>Issuer - Sector</b>	<b>% of Net Assets</b>
<b>Celgene Corporation</b> <i>Biotechnologies/Biopharmaceuticals</i>	5.04%
<b>Amgen Inc.</b> <i>Biotechnologies/Biopharmaceuticals</i>	3.96%
<b>Biogen Idec Inc.</b> <i>Biotechnologies/Biopharmaceuticals</i>	3.61%
<b>Genzyme Corporation</b> <i>Biotechnologies/Biopharmaceuticals</i>	3.35%
<b>Vertex Pharmaceuticals Inc.</b> <i>Biotechnologies/Biopharmaceuticals</i>	3.35%
<b>Teva Pharmaceutical Industries, Ltd.</b> <i>Generic Pharmaceuticals</i>	3.25%
<b>Illumina, Inc.</b> <i>Medical Devices and Diagnostics</i>	3.11%
<b>United Therapeutics Corporation</b> <i>Biotechnologies/Biopharmaceuticals</i>	2.57%
<b>Cephalon, Inc.</b> <i>Biotechnologies/Biopharmaceuticals</i>	2.46%
<b>Concentric Medical, Inc.</b> <i>Medical Devices and Diagnostics</i>	2.13%

### PORTFOLIO

As of September 30, 2009



## H&Q LIFE SCIENCES INVESTORS

### SCHEDULE OF INVESTMENTS

SEPTEMBER 30, 2009

<b>CONVERTIBLE SECURITIES AND WARRANTS - 11.0% of Net Assets</b>		
<b>SHARES</b>	<b>Convertible Preferred (Restricted) <sup>(a)</sup></b>	<b>VALUE</b>
	<b>(b) - 10.7%</b>	
	<i>Biotechnologies/Biopharmaceuticals - 0.7%</i>	
204,275	MacroGenics, Inc. Series D	\$ 133,208
	MacroGenics, Inc. Series D 18	
50,145	Month Lock-up	21,798
1,415,385	TargeGen, Inc. Series C	1,226,672
407,825	TargeGen, Inc. Series D	353,450
		1,735,128
	<i>Drug Discovery Technologies - 1.3%</i>	
1,587,302	Agilix Corporation Series B <sup>(c)</sup>	94,540
250,000	Ceres, Inc. Series C	1,625,000
21,462	Ceres, Inc. Series C-1	139,503
175,540	Ceres, Inc. Series D	1,141,010
28,385	Ceres, Inc. Series F	184,502
5,677	Ceres, Inc. warrants (expiration 9/05/15)	0
		3,184,555
	<i>Healthcare Services - 1.4%</i>	
3,589,744	PHT Corporation Series D <sup>(c)</sup>	2,800,000
802,996	PHT Corporation Series E <sup>(c)</sup>	626,337
99,455	PHT Corporation Series F <sup>(c)</sup>	77,575
		3,503,912
	<i>Medical Devices and Diagnostics - 7.3%</i>	
2,379,916	CardioKinetix, Inc. Series C	1,640,000
3,235,293	Concentric Medical, Inc. Series B <sup>(c)</sup>	3,235,293
1,162,790	Concentric Medical, Inc. Series C <sup>(c)</sup>	1,162,790
455,333	Concentric Medical, Inc. Series D <sup>(c)</sup>	455,333
453,094	Concentric Medical, Inc. Series E <sup>(c)</sup>	453,094
1,198,193	Elemé Medical, Inc. Series C	632,646
1,592,852	FlowCardia, Inc. Series C	1,708,334
1,304,545	Interlace Medical, Inc. Series C	1,435,000
2,446,016	Labcyte Inc. Series C	1,280,000
2,050,000	Magellan Biosciences, Inc. Series A	2,050,000
	Magellan Biosciences, Inc. warrants	
98,824	(expiration 4/01/19)	0
	Magellan Biosciences, Inc. warrants	
7,877	(expiration 5/06/19)	0
	OmniSonic Medical Technologies, Inc.	
1,031,992	Series A-1	1,031
877,747	OmniSonic Medical Technologies, Inc.	877

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	Series B-1	
	Palyon Medical Corporation Series	
9,606,373	A <sup>(c)</sup>	2,050,000
43,478	TherOx, Inc. Series H	72,122
99,646	TherOx, Inc. Series I	165,293

The accompanying notes are an integral part of these financial statements.

## H&Q LIFE SCIENCES INVESTORS

### SCHEDULE OF INVESTMENTS

SEPTEMBER 30, 2009

(continued)

SHARES	Convertible Preferred (Restricted) <sup>(a) (b)</sup> - continued	VALUE
2,813	TherOx, Inc. warrants (expiration 1/26/11)	\$ 0
5,427	TherOx, Inc. warrants (expiration 6/09/10)	0
640,625	Xoft, Inc. Series D	1,601,562
122,754	Xoft, Inc. Series E	306,885
N/A	Xoft, Inc. warrants (expiration 6/12/14) <sup>(d)</sup>	0
		18,250,260
		\$ 26,673,855
PRINCIPAL AMOUNT	Convertible Notes - 0.3%	
	<i>Biotechnologies/Biopharmaceuticals - 0.0%</i>	
\$ 76,202	TargeGen, Inc., Promissory Note, 8.00% due 2010 (Restricted) <sup>(a)</sup>	76,202
	<i>Drug Discovery Technologies - 0.1%</i>	
700,000	deCODE Genetics, Inc., 3.50% due 2011	103,250
	<i>Medical Devices and Diagnostics - 0.2%</i>	
106,701	Magellan Biosciences, Inc., Senior Subordinated Notes, 8.00% due 2010 (Restricted) <sup>(a)</sup>	106,701
410,000	Xoft, Inc., Promissory Note, 10.00% due 2010 (Restricted) <sup>(a)</sup>	410,000
		516,701
		\$ 696,153
	<b>TOTAL CONVERTIBLE SECURITIES AND WARRANTS</b> (Cost \$35,346,510)	\$ 27,370,008
	<b>COMMON STOCKS AND WARRANTS - 84.3%</b>	
	<b>Biotechnologies/Biopharmaceuticals - 44.0%</b>	
SHARES		
130,764	Acorda Therapeutics Inc. <sup>(b)</sup>	3,044,186
135,182	Affymax, Inc. <sup>(b)</sup>	3,229,498
8,200	Alexion Pharmaceuticals, Inc. <sup>(b)</sup>	365,228
165,506	Alnylam Pharmaceuticals, Inc. <sup>(b)</sup>	3,753,676
56,000	AMAG Pharmaceuticals, Inc. <sup>(b)</sup>	2,446,080
163,562	Amgen Inc. <sup>(b)</sup>	9,851,339
202,959	Amylin Pharmaceuticals, Inc. <sup>(b)</sup>	2,778,509
3,588,710	Antisoma plc <sup>(b) (e)</sup>	2,023,210
340,305	Antisoma plc 18 Month Lock-up (Restricted) <sup>(a) (b) (e)</sup>	182,261

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328,000	Athersys, Inc. <sup>(b)</sup>	400,160
82,000	Athersys, Inc. warrants (Restricted, expiration 6/08/12) <sup>(a) (b)</sup>	1,640

The accompanying notes are an integral part of these financial statements.

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## H&Q LIFE SCIENCES INVESTORS

### SCHEDULE OF INVESTMENTS

SEPTEMBER 30, 2009

(continued)

SHARES	Biotechnologies/ Biopharmaceuticals - continued	VALUE
177,728	Biogen Idec Inc. <sup>(b)</sup>	\$ 8,978,819
131,000	BioMarin Pharmaceutical Inc. <sup>(b)</sup>	2,368,480
224,236	Celgene Corporation <sup>(b)</sup>	12,534,792
105,114	Cephalon, Inc. <sup>(b)</sup>	6,121,839
174,224	Cornerstone Therapeutics Inc. <sup>(b)</sup>	1,141,167
	Cornerstone Therapeutics Inc. warrants	
15,967	(Restricted, expiration 6/06/10) <sup>(a) (b)</sup>	319
203,897	Cubist Pharmaceuticals, Inc. <sup>(b)</sup>	4,118,719
51,257	Dendreon Corporation <sup>(b)</sup>	1,434,683
	DOV Pharmaceutical, Inc. warrants (Restricted, expiration 12/31/09) <sup>(a)</sup>	
90,552	<sup>(b)</sup>	0
147,001	Genzyme Corporation <sup>(b)</sup>	8,339,367
100,625	Gilead Sciences, Inc. <sup>(b)</sup>	4,687,113
153,000	Isis Pharmaceuticals, Inc. <sup>(b)</sup>	2,229,210
157,476	Martek Biosciences Corporation <sup>(b)</sup>	3,557,383
132,850	Medicines Company <sup>(b)</sup>	1,462,679
	MiddleBrook Pharmaceuticals, Inc. warrants	
175,880	(Restricted, expiration 4/29/10) <sup>(a) (b)</sup>	3,518
75,811	Onyx Pharmaceuticals, Inc. <sup>(b)</sup>	2,272,056
48,190	OSI Pharmaceuticals, Inc. <sup>(b)</sup>	1,701,107
148,886	Regeneron Pharmaceuticals, Inc. <sup>(b)</sup>	2,873,500
130,651	United Therapeutics Corporation <sup>(b)</sup>	6,400,593
220,017	Vertex Pharmaceuticals Inc. <sup>(b)</sup>	8,338,644
131,293	XenoPort, Inc. <sup>(b)</sup>	2,787,350
		109,427,125
	<b>Drug Delivery - 2.1%</b>	
163,552	Alkermes, Inc. <sup>(b)</sup>	1,503,043
997,671	DURECT Corporation <sup>(b)</sup>	2,663,782
394,928	Penwest Pharmaceuticals Co. <sup>(b)</sup>	825,399
	Penwest Pharmaceuticals Co. warrants	
199,514	(Restricted, expiration 3/11/13) <sup>(a) (b)</sup>	185,548
		5,177,772
	<b>Drug Discovery Technologies - 0.1%</b>	
7,627	Clinical Data, Inc. <sup>(b)</sup>	127,142
162,288	Clinical Data, Inc. CVR (Restricted) <sup>(a) (b) (f)</sup>	25,430
1,601,039	MZT Holdings, Inc. <sup>(b) (c)</sup>	48,031
1,846,154		