

H&Q LIFE SCIENCES INVESTORS
Form N-CSRS
June 05, 2009

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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 March 31, 2009

ITEM 1. REPORTS TO STOCKHOLDERS.

H&Q LIFE SCIENCES INVESTORS

Semiannual Report

March 31, 2009

(Unaudited)

To our Shareholders:

On March 31, 2009, the net asset value (NAV) per share of the Fund was \$10.11. During the six month period ended March 31, 2009, total return at NAV of your Fund was -18.58%, with distributions reinvested. During the most recent quarter ended March 31, 2009, total return at NAV of your Fund was -3.42%, with distributions reinvested. The total investment return at market with distributions reinvested was -22.04% during the six month period ended March 31, 2009 and was -7.12% during the quarter ended March 31, 2009. Comparisons to relevant indices are listed below:

Investment Returns	Three Months Ended 3/31/09	Six Months Ended 3/31/09
Investment Return at Market	-7.12%	-22.04%
Net Asset Value	-3.42%	-18.58%
NASDAQ Biotech Index (NBI)	-6.41%	-18.33%
S&P 500 Index	-11.01%	-30.54%

While we typically focus on individual company fundamentals, macroeconomic events have played an unusually large role in how we managed the Fund during the last six months. As I am sure you are aware, virtually all sectors of the market have been dramatically impacted by the credit crunch and by the economic recession that has dominated the news during the six month period ended March 31, 2009. Within the Fund's portfolio, for example, several medical device companies with products in the aesthetics and/or capital equipment sectors seem to be particularly affected. As noted above, both the broad market and the healthcare sector have been down over this six month period. For much of the period, fundamentals appear to be secondary to credit availability and other factors affecting stock price movement. From our view, good companies those with growing products and solid balance sheets were taken down along with other less fundamentally strong companies. On the way down to the March 2009 lows, we sought to minimize losses by selling portions of the Fund's positions in what we believed were relatively weaker companies. As you know, over the last several years we have decreased our weighting of the smallest healthcare companies. We believe that, as a whole, this group (typified by non-profitable, development-stage companies) will continue to struggle to acquire needed access to investment funding and will under-perform the broader healthcare market. As the market has stabilized in March, we have cautiously begun to increase and accumulate positions in companies we think have longer-term potential for stock appreciation.

We do not think the market is on an inevitable upward climb, but we are cautiously optimistic that we have seen the bottom. At this point, our biggest concern is macroeconomic. We continue to be concerned about the financial sector in general and housing in particular. We are concerned that as the government slowly retreats from assertive support of financials and voluntary moratoria on housing foreclosures are lifted, there is a real chance that we will see another significant sharp decline in the markets. We are cautiously optimistic though that we have seen the stock market low. In our experience, fear drives over-selling and it looks to us that the general fear of broad economic system collapse, prevalent during the fourth quarter of 2008, has waned. The overall market does not look cheap to us at this point, but based on our assumptions about future earnings, it also does not look significantly overpriced.

We believe that similar fears have been a factor in the healthcare sector. As described above, healthcare (as generally represented by the NBI) outperformed the broader market during the six month period ended March 31, 2009. However, on an absolute basis, the NBI declined precipitously during a two week period around March 1, 2009. This decline immediately followed the release of the new Administration's proposed 2010 fiscal budget. It is our opinion that this decline was effected in significant part by fears that the healthcare sector would be disproportionately and negatively affected by implementation of many aspects of the President's healthcare agenda, including ultimately the creation of a single-payer system. We think that this response was an overreaction. In fact, the NBI has recovered somewhat since the March 9, 2009 low. Over time a single-payer option may well be created, but in our judgment the managed care industry will play a significant part in the creation and/or implementation of such a program. We do not think that the managed care group will be disenfranchised by the Administration's planned actions, as some appear to think. We also feel that there will be both winners and losers as a result of changes in the way healthcare, both clinically and on the R&D side, is administered. For example, given the Administration's intention to significantly increase the National Institute of Health's research budget, we agree with the commonly held belief that companies in the life sciences tools area will benefit at least incrementally. We also agree that companies that make large equipment (e.g., radiology and robotics systems) may face headwinds, but that is more an effect of the macro economy than of any government policy change. The magnitude of any impact on capital equipment is also likely to be very much company- and product-dependent.

Beyond macroeconomics, we note that the magnitude and breadth of merger and acquisition activity within the healthcare sector has been dramatic in recent months. A number of large bellwether companies such as Pfizer Inc. (which committed to acquire Wyeth), Merck & Co., Inc. (which committed to acquire Schering-Plough Corporation), Roche Holding AG (which acquired Genentech, Inc.) and Abbott Laboratories (which committed to acquire Advanced Medical Optics) have participated. Notable mid-sized companies, such as Gilead Sciences, Inc. (which acquired CV Therapeutics, Inc.) also participated in this trend. A number of smaller transactions also occurred. This wave of M&A activity has led to some speculation about "which company is next?" and has resulted in short term price movement, both up and down, for the stocks of companies that investors speculate might be takeover candidates. In general, as more fundamental analysts, we have avoided acting on such speculation. On occasion though, we have taken advantage of speculation by others to sell positions in companies which we think are over-priced based on fundamentals.

As we have previously mentioned, we also see diagnostics as an area for growth in both the near and intermediate term. We believe that diagnostics hold the promise of delivering better and more cost effective treatment of patients, by tailoring the delivery of specific treatments to particular patients in need. For example, Myriad Genetics, Inc., a Fund holding, markets a test that evaluates the presence of specific breast cancer "markers". This test is currently used in determining a woman's long-term risk of cancer and helps to determine whether a woman with breast cancer should receive a treatment that has been shown to be more effective in the presence of the marker than in its absence. By avoiding treatment in women whose tumors lack the marker, the cost and side effects of the treatment can be avoided. Overall, this approach is becoming more common and should benefit specific patients and the healthcare system in general.

Finally we note that, as always, the healthcare sector has seen both encouraging and discouraging clinical events in recent months. The failure of Genentech's (now Roche's) Avastin product in the adjuvant colorectal cancer setting was one of the more disappointing events of recent years. Many observers had anticipated success. On the other hand, Vertex Pharmaceutical Inc.'s Phase II clinical data with its telaprevir product suggest that this product could well represent a breakthrough in the treatment of hepatitis.

During the six month period ended March 31, 2009, within the public portfolio, the Fund established positions in several holdings

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including Alexion Pharmaceuticals, Inc., Cephalon, Inc., Illumina, Inc., iShares Nasdaq Biotechnology Index, an exchange-traded fund, and Monsanto Company. During the same six month period the Fund exited its positions in several holdings including Baxter International Inc., BioMarin Pharmaceutical Inc., Genentech, Inc., Omrix Biopharmaceuticals, Inc. and Thermo Fisher Scientific Inc.

During the six month period ended March 31, 2009, within the venture portfolio, the Fund made a follow-on investment in Concentric Medical, Inc. Series E. The Fund exited its position in Cytologix, Inc. and wrote off its investment in EPR, Inc.

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 March 31, 2009
(Unaudited)

	% of Net Assets
Gilead Sciences, Inc.	7.1%
Celgene Corporation	4.7%
Teva Pharmaceutical Industries, Ltd.	4.3%
Genzyme Corporation	4.1%
Biogen Idec Inc.	4.0%
Amgen Inc.	3.9%
CardioNet, Inc.	3.0%
iShares Nasdaq Biotechnology Index Fund	2.6%
United Therapeutics Corporation	2.6%
Concentric Medical, Inc.	2.4%

H&Q LIFE SCIENCES INVESTORS

PORTFOLIO

As of March 31, 2009
(Unaudited)

H&Q LIFE SCIENCES INVESTORS

SCHEDULE OF INVESTMENTS

MARCH 31, 2009

(Unaudited)

CONVERTIBLE SECURITIES AND WARRANTS - 11.0% of Net Assets		
SHARES	Convertible Preferred (Restricted) ^(a) - 11.0%	VALUE
	<i>Drug Discovery Technologies - 1.4%</i>	
1,587,302	Agilix Corporation Series B ^{(b)(c)}	\$ 94,540
250,000	Ceres, Inc. Series C ^(b)	1,625,000
21,462	Ceres, Inc. Series C-1 ^(b)	139,503
175,540	Ceres, Inc. Series D ^(b)	1,141,010
28,385	Ceres, Inc. Series F ^(b)	184,502
5,677	Ceres, Inc. warrants (expiration 9/05/15) ^(b)	0
	<i>Emerging Biopharmaceuticals - 0.8%</i>	
204,275	MacroGenics, Inc. Series D ^(b)	133,208
50,145	MacroGenics, Inc. Series D ^(b)	21,798
1,415,385	TargeGen, Inc. Series C ^(b)	1,226,672
407,825	TargeGen, Inc. Series D ^(b)	353,450
	<i>Healthcare Services - 1.6%</i>	
3,589,744	PHT Corporation Series D ^{(b)(c)}	2,800,000
802,996	PHT Corporation Series E ^{(b)(c)}	626,337
99,455	PHT Corporation Series F ^{(b)(c)}	77,575
	<i>Medical Devices and Diagnostics - 7.2%</i>	
2,379,916	CardioKinetix, Inc. Series C ^{(b)(c)}	1,640,000
3,235,293	Concentric Medical, Inc. Series B ^{(b)(c)}	3,235,293
1,162,790	Concentric Medical, Inc. Series C ^{(b)(c)}	1,162,790
455,333	Concentric Medical, Inc. Series D ^{(b)(c)}	455,333
453,094	Concentric Medical, Inc. Series E ^{(b)(c)}	453,094
1,198,193	Elemé Medical, Inc. Series C ^(b)	805,665
1,592,852	FlowCardia, Inc. Series C ^(b)	1,708,334
2,446,016	Labcyte Inc. Series C ^(b)	1,280,000
2,050,000	Magellan Biosciences, Inc. Series A ^(b)	2,050,000
1,031,992	OmniSonics Medical Technologies, Inc. Series A-1 ^(b)	1,031
877,747	OmniSonics Medical Technologies, Inc. Series B-1 ^(b)	877
43,478	TherOx, Inc. Series H ^(b)	144,243
99,646	TherOx, Inc. Series I ^(b)	330,586
2,813	TherOx, Inc. warrants (expiration 1/26/10) ^(b)	0
5,427	TherOx, Inc. warrants (expiration 6/09/09) ^(b)	0
640,625	Xoft, Inc. Series D ^(b)	2,139,688
122,754	Xoft, Inc. Series E ^(b)	409,998
		\$ 24,240,527

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

H&Q LIFE SCIENCES INVESTORS**SCHEDULE OF INVESTMENTS**

MARCH 31, 2009

(Unaudited)

(continued)

PRINCIPAL AMOUNT	Convertible Notes - 0.0%	VALUE
	<i>Drug Discovery Technologies - 0.0%</i>	
\$ 700,000	deCODE Genetics, Inc., 3.50% due 2011	\$ 21,000
	TOTAL CONVERTIBLE SECURITIES AND WARRANTS	
	(Cost \$31,241,836)	\$ 24,261,527
SHARES	COMMON STOCKS AND WARRANTS - 80.4%	
	Agricultural Chemicals - 2.1%	
55,800	Monsanto Company	4,636,980
	Biopharmaceuticals - 33.4%	
135,182	Affymax, Inc. ^(b)	2,177,782
823,996	Akorn, Inc. ^(b)	708,637
108,889	Akorn, Inc. warrants (expiration 3/08/11) ^{(a) (b)}	34,845
124,024	Alexion Pharmaceuticals, Inc. ^(b)	4,670,744
42,700	Alnylam Pharmaceuticals, Inc. ^(b)	813,008
173,062	Amgen Inc. ^(b)	8,570,030
55,000	Amylin Pharmaceuticals, Inc. ^(b)	646,250
525,965	Antisoma plc ^{(b) (d)}	199,781
3,062,745	Antisoma plc 12 Month Lock-up (Restricted) ^{(a) (b) (d)}	1,047,012
340,305	Antisoma plc 18 Month Lock-up (Restricted) ^{(a) (b) (d)}	109,872
168,068	Biogen Idec Inc. ^(b)	8,810,125
75,627	Cornerstone Therapeutics Inc. ^(b)	310,071
15,967	Cornerstone Therapeutics Inc. warrants (expiration 6/06/10) ^{(a) (b)}	6,227
111,795	Cubist Pharmaceuticals, Inc. ^(b)	1,828,966
88,550	Forest Laboratories, Inc. ^(b)	1,944,558
151,728	Genzyme Corporation ^(b)	9,011,126
336,725	Gilead Sciences, Inc. ^(b)	15,597,102
182,994	Hologic, Inc. ^(b)	2,395,391
8,815	Intuitive Surgical, Inc. ^(b)	840,598
52,917	Martek Biosciences Corporation	965,735
82,850	Medicines Company ^(b)	898,094
175,880	MiddleBrook Pharmaceuticals, Inc. warrants (expiration 4/29/10) ^{(a) (b)}	52,764
78,098	Myriad Genetics, Inc. ^(b)	3,551,116
168,570	Vertex Pharmaceuticals Inc. ^{(b) (e)}	4,843,016
29,500	Wyeth	1,269,680
102,371	XenoPort, Inc. ^(b)	1,981,903

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7

H&Q LIFE SCIENCES INVESTORS**SCHEDULE OF INVESTMENTS**

MARCH 31, 2009

(Unaudited)

(continued)

	SHARES	VALUE
	Biotechnology - 1.8%	
328,000	Athersys, Inc. ^(b)	\$ 295,200
82,000	Athersys, Inc. warrants (expiration 6/08/12) ^(a) ^(b)	820
109,402	Life Technologies Corporation ^(b)	3,553,377
		3,849,397
	Drug Delivery - 0.6%	
113,800	Alkermes, Inc. ^(b) ^(c)	1,380,394
	Drug Discovery Technologies - 12.6%	
162,288	Avalon Pharmaceuticals, Inc. ^(b)	73,030
231,236	Celgene Corporation ^(b)	10,266,878
43,631	Cephalon, Inc. ^(b)	2,971,271
44,975	Cougar Biotechnology, Inc. ^(b)	1,448,195
1,601,039	MZT Holdings, Inc. ^(b) ^(c)	40,026
1,846,154	MZT Holdings, Inc. warrants (expiration 1/17/11) ^(a) ^(b) ^(c)	0
952,381	MZT Holdings, Inc. warrants (expiration 1/22/12) ^(a) ^(b) ^(c)	0
70,740	OSI Pharmaceuticals, Inc. ^(b)	2,706,512
399,028	Penwest Pharmaceuticals Co. ^(b)	654,406
199,514	Penwest Pharmaceuticals Co. warrants (expiration 3/11/13) ^(a) ^(b)	215,475
97,410	Pfizer Inc.	1,326,724
97,200	Pharmaceutical Product Development, Inc.	2,305,584
84,700	United Therapeutics Corporation ^(b)	5,597,823
46	Zyomyx, Inc. (Restricted) ^(a) ^(b)	12
		27,605,936
	Emerging Biopharmaceuticals - 1.5%	
430,995	ACADIA Pharmaceuticals Inc. ^(b)	409,445
90,552	DOV Pharmaceutical, Inc. warrants (expiration 12/31/09) ^(a) ^(b)	0
426,380	Exelixis, Inc. ^(b)	1,961,348
774,191	Lexicon Pharmaceuticals, Inc. ^(b)	843,868
242,522		