PitchBook

European Venture Report

3Q 2018

PitchBook

Contents

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Key takeaways from the analysts

VCs invested €4.5 billion across 584 deals in Europe in 3Q, marking a slowdown in dealmaking after heavy activity in the first half of 2018. At the current pace, we expect to see 2018 deal value match or top 2017 in terms of capital invested, albeit likely across fewer deals. Fierce competition among investors has provided startups flexibility in funding options, while exerting upward pressure on deal sizes and valuations.

A favorable exit environment has been a welcome development for investors, as 3Q saw €7.2 billion exited through 67 deals. This moves YTD exit value to €20 billion, already the highest annual total since 2014. Much of the current year's strength can be attributed to an open IPO window that has facilitated public listing of several billion-euro businesses.

VCs raised €2.0 billion in the third quarter, a 5.4% decline from the quarter prior; however, strong overall fundraising in 2018 suggests annual figures will surpass 2017. Fund count was depressed for the second straight quarter with 13 funds closed. 49 funds were closed over the first three quarters, a 16.9% decline year over year, and a continuation of a trend toward fewer and larger funds; a 54.6% rise in median fund size YoY helps to illustrate this trend.

€4.5B
total deal value across 584 deals in 3Q 2018

€7.2B
total exit value across 67 exits in 3Q 2018

€2.0B
total capital raised across 13 funds in 3Q 2018

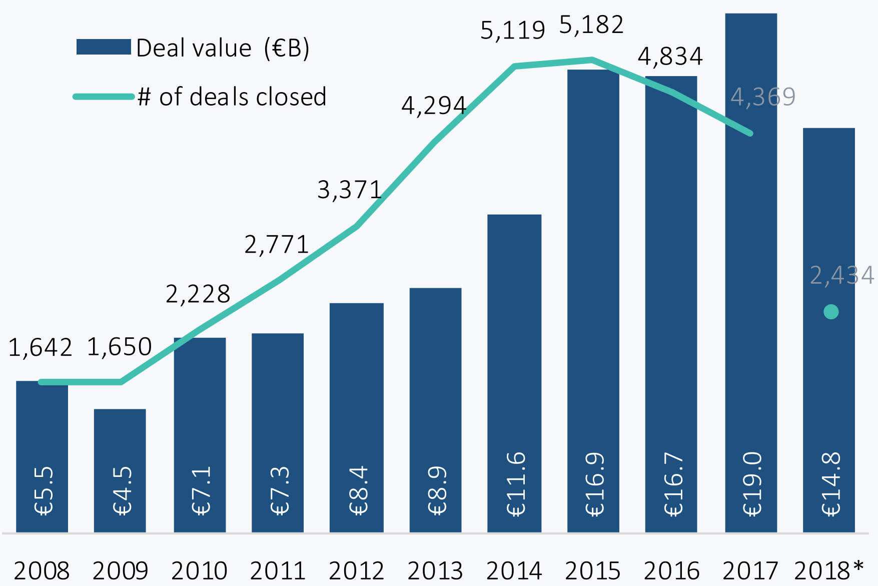
Overview

European VC deal activity in 3Q came in slightly below the levels we saw through the first half of 2018, breaking a three-quarter streak of at least €5 billion invested. VCs completed 584 deals during 3Q, placing €4.5 billion into European startups. At the current pace, we expect to see 2018 deal value match or top 2017 in terms of capital invested, albeit likely across fewer deals.

Median deal sizes advanced across the board, with significant jumps over 2017's value at the early (85.4%) and late (64.2%) stages. Investors continue to seek out and invest into growing companies, which is one factor pushing valuations and deal sizes higher. Competition remains fierce too, as startups currently enjoy access to a diverse set of funding options, especially with investment interest from corporations.

VCs continue to deploy capital at a record pace

European VC deal activity



Source: PitchBook
*As of September 30, 2018

The downturn of angel & seed financings endured in 3Q, with double-digit percentage declines in value and count. This trend began at the start of 2016, and while it looked like we recently had found a stable level of deal value, activity continued to grind lower in 3Q. We've also seen more investors choosing to raise larger funds, the sizes of which can make it more difficult to efficiently allocate capital to angel & seed deals. Due to this phenomenon, much of the slack has been picked up by early-stage deals, as companies find more support from investors at that stage of the lifecycle.

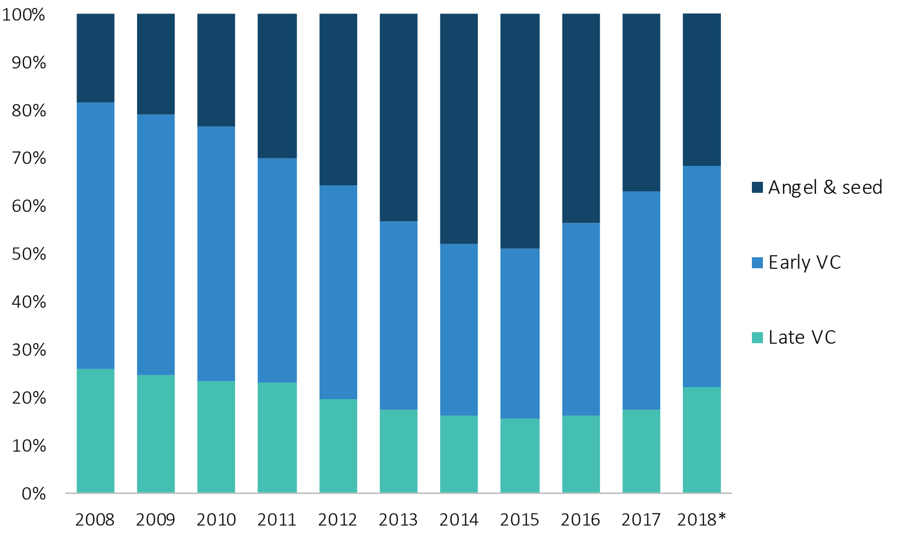
Capital invested into the early stage in 3Q was the highest of any stage as larger deals become the norm regardless of company age. Early-stage companies received €2.3 billion across 295 deals during the quarter, marking back-to-back quarters of over €2.0 billion invested into the early stage. Early-stage deals have remained the category with the highest deal counts after surpassing angel & seed counts in 2017.

Interestingly, late-stage investment was relatively subdued in the third quarter, resulting in nearly €2.0 billion invested across 152 deals. This deal count was relatively in line with what we've seen over the past two years but lacked the grouping of outsized deals to drive deal value growth. This relationship between the early and late stages sits in stark contrast with what we see in the US VC ecosystem where late-stage deal value is regularly more than three times the early stage. From our perspective, the major difference is a current lack of widespread VC support or ability to do €100 million+ deals. This has become a staple of the US VC playbook but is still relatively rare in Europe.

3Q's early-stage deals were headlined by the €257 million fundraise by German ecommerce company About You, as well as a pair of blockchain companies based in Zug, Switzerland that each raised more than €85 million.

Late-deals account for a growing share of activity

European VC deals (#) by stage



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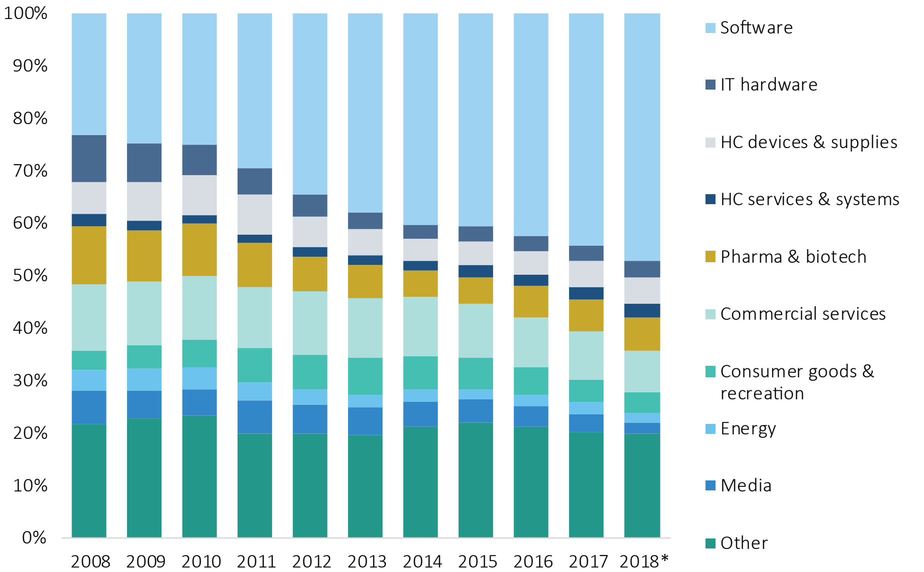
*As of September 30, 2018

Software is the bedrock of VC investment

European VC deals (#) by sector



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Dfinity, which attracted investment from major Silicon Valley blockchain investors, including Andreesen Horowitz and Polychain Capital, is seeking to provide a decentralized cloud computing resource. SEBA Crypto is a blockchain application that builds banking-type services for cryptocurrency, including ICO advisory and more corporate financing support.

Although cryptocurrency prices have experienced a marked decline during 2018, investors are still seeing value in the technology underlying these financial advancements. As blockchain technology is quite nascent, it will be interesting to witness the continued development of the technology along with VC investors interest in backing these projects inside and outside of Europe.

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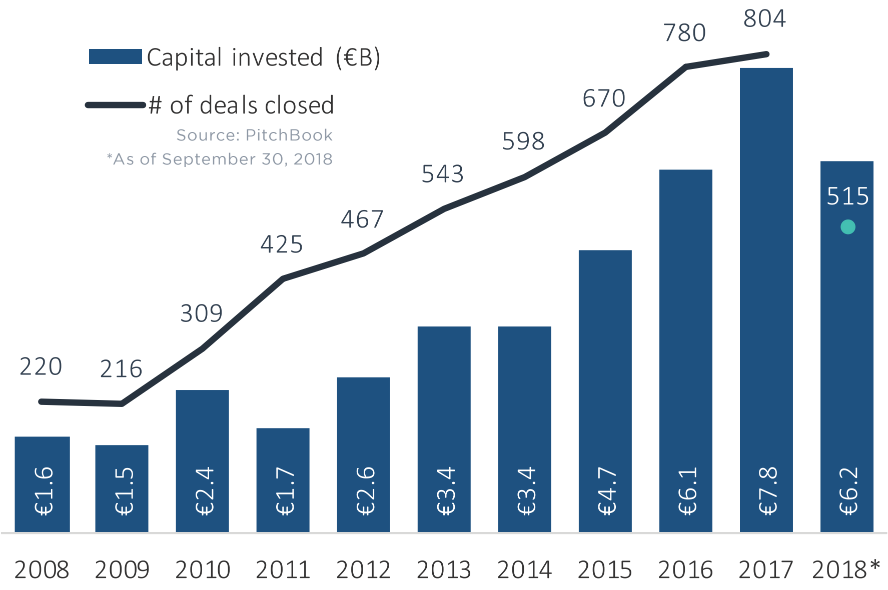
Corporate VC

Corporate VC (CVC) participation is tracking for another record year; through three quarters, corporations have participated in 515 deals representing over €6.2 billion in deal value, a 12.5% increase in value over the first three quarters of 2017. Capital invested has already surpassed 2016 full-year totals and is pacing to surpass 2017, too. This is largely attributable to a steady rise in the median European CVC deal size over the past four years—a trend that has accelerated sharply in 2018, with every stage (except Series A) seeing double-digit percentage increases over the first three quarters of 2018. At the same time, deals less than €5 million have seen a proportionate decline, with investors shifting toward larger check sizes.

CVCs on track for another record year

European VC deal activity with CVC participation

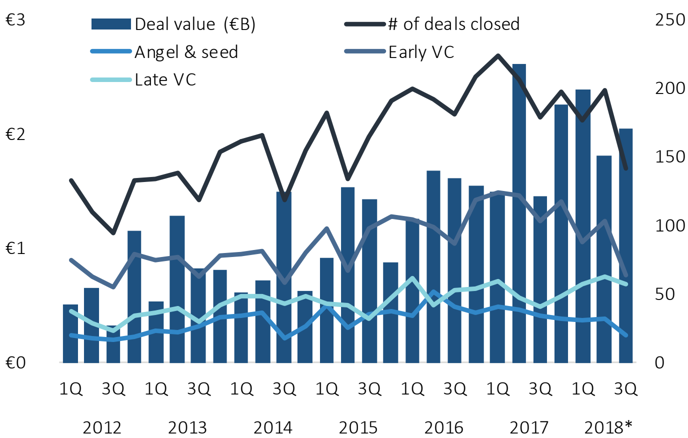


Late-stage participation by corporations has been the steadiest on a deal count basis over the past two years, which is in line with where corporations' investment objectives usually lie. With a more market-oriented approach, CVC investment has often focused on companies that have demonstrated commercial viability, which is commonly true of late-stage companies. However, as the VC environment has matured, companies are generating revenue sooner than they had in the past, enabling earlier participation by corporations. Illustrating this point, the median deal size with CVC participation regardless of stage is currently €6.1 million, 144% higher than the broader market median, confirming that CVC's are backing more mature companies even across the early stage.

The largest CVC deal of the quarter, About You's €256 million early-stage financing, serves as a quintessential example of corporate involvement in the VC landscape. The company, a fashion technology company operating as a subsidiary of German retailing giant Otto Group, reached a valuation of €1 billion with this latest deal from more corporate investors, including SevenVentures and Bestseller A/S. As large businesses seek to innovate and avoid disruption, more corporations have turned to involvement with startups to unlock growth opportunities. Especially with the fickleness of consumers in the retail setting, corporations must quickly adapt to the desires of consumers, which can be easier through external investments or partnerships.

Capital invested stays strong, despite dip in deals

European VC deal activity with CVC participation



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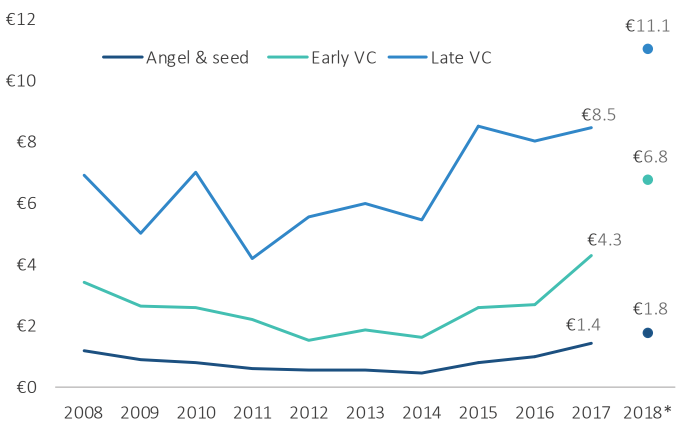
Deal sizes reach new heights

Median European VC deal size (€M) with CVC participation by stage



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Regional spotlight: UK & Ireland

The UK & Ireland region has long been the leader of venture activity in Europe. Firms in the region have garnered the majority of deal activity every quarter for the last nine years. In the first three quarters of 2018, 39.0% of European VC deals were raised by companies in the region. Capital raised has steadily increased over the past decade and is on pace to achieve over €6.7 billion in 2018. In line with larger European trends, activity in the UK & Ireland region is also progressing toward fewer yet larger deals.

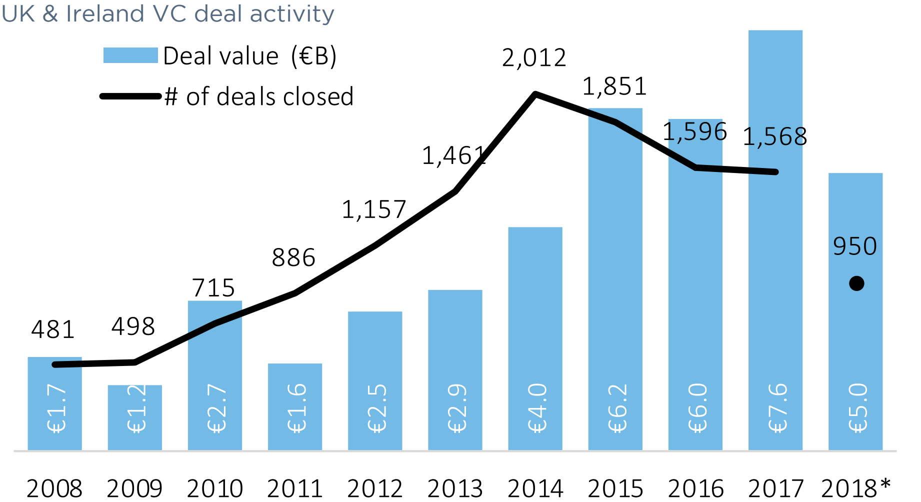
The impressive ascent in capital raised over the past six years has been tempered by a decline in deal count and capital raised thus far in 2018. The slowdown in capital raised is due in part to a shortage of larger deals. Firms such as Improbable and Deliveroo closed sizable deals in 2017, but no firm in 2018 has closed any deals more than €250 million. Deal count is down 23% through 3Q YoY and currently rests at 213 deals closed in 3Q and 950 deals closed YTD.

UK leads capital raised in the region. An average of over 90% of capital invested has been raised by UK startups over the past five years. And over 88% of the deals were directed into UK companies over the same timeframe. This can be attributed to London's status as an international financial hub and the associated talent and capital this brings.

Despite the slight dip in dealmaking across UK & Ireland this year, exits have achieved a new high with 2.5x more exit value than in 2017. This is largely due to an uptick in IPOs. Farfetch, an ecommerce platform for independent boutiques, went public at $20 per share to raise $884.9 million. The next largest exit was by Funding Circle, an online marketplace for business loans. The London-based firm raised €574.4 million.

Capital investment exceeds €5B for fourth straight year

UK & Ireland VC deal activity



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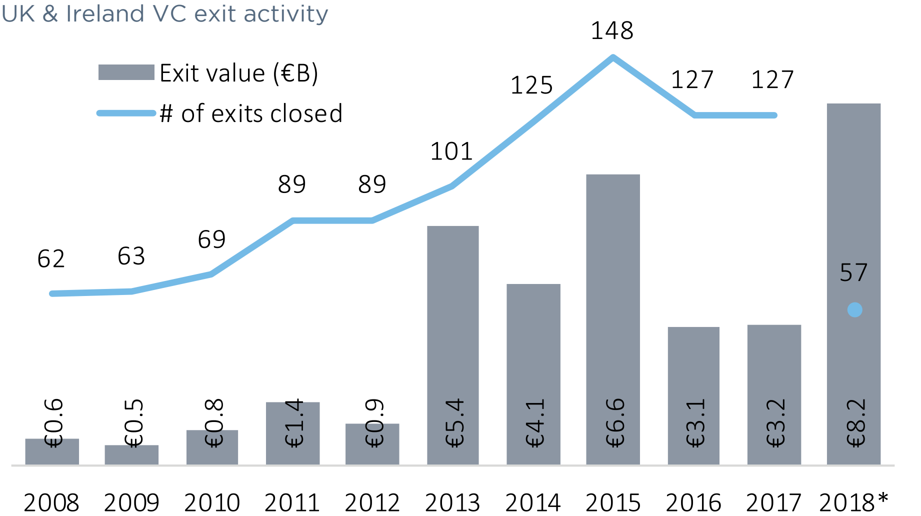
Exit value at a record thanks to Farfetch's IPO

UK & Ireland VC exit activity



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*As of September 30, 2018

Fundraising for new vehicles has been operating at elevated levels over the past six years with capital raised picking up notably over the first two quarters of 2018. Despite a disappointing 3Q, we expect funding to surpass 2017 levels and possibly reach a new high in 2018. The largest fund closed in 2018 was the €463.0 million vehicle raised by Highland Europe. One of the most interesting funds closed in 2018 is a €283.1 million vehicle called the Dementia Discovery Fund. The fund, which is backed by the British government as well as a consortium of pharma firms, aims to invest in firms focused on preclinical research activities related to dementia. The government's active support and participation in this asset class signals its initiative to encourage the formation of unique and targeted venture funds amid the recent slowed fundraising activity.

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Exits

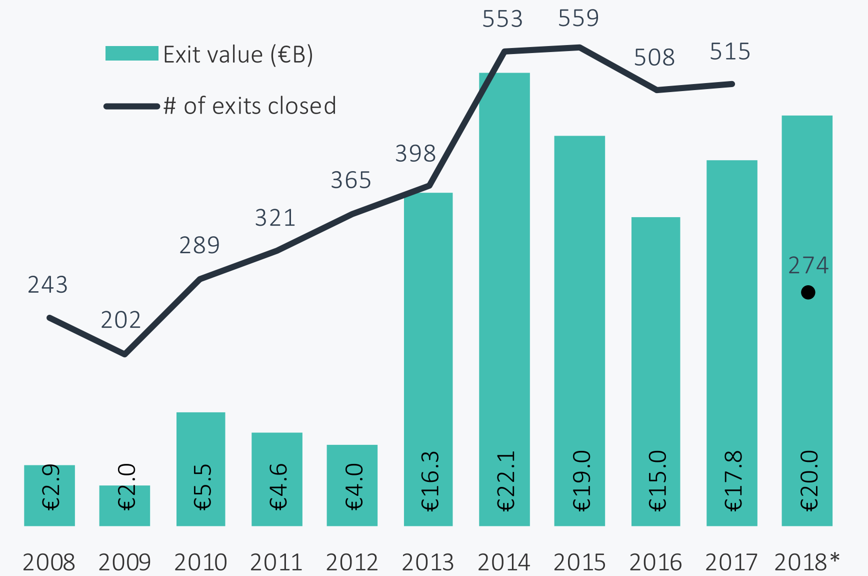
Exit activity has been a bright spot in 2018, easily topping 2017's annual value through three quarters. 3Q saw €7.2 billion exited through 67 deals, moving YTD value exited to €20 billion, already the highest total since 2014. If 4Q proves to be another strong quarter from the exit market, 2018 has a very realistic opportunity to see the most exit value in a single year. This trend is assisted by the increasing commonality of larger exits driving the VC ecosystem. VC has always had a focus on few "home-run" exits driving a majority of the return for a given fund. This trend has become only more apparent over the last few years, with exits more than €100 million accounting for anywhere between 75% and 92% of total exit value over the last six years, with 2018 representing the most extreme data point.

Much of the current year's strength has been through the open IPO window and several billion-euro businesses that chose to list on the public markets throughout the year. It is also worth noting that we have updated our methodology to include the pre-money valuation of the listing company as the exit value rather than the amount raised in the IPO, which accounts for the value of the entire business and makes the figure more comparable to the value of acquired companies. While this change has increased exit values across every year, 2014 and 2018 saw the most improvement due to the timing of outsized IPOs.

Illustrating this point, the two largest exits of 3Q were both IPOs of London-based companies valued at more than €1 billion: Farfetch and Funding Circle. Both firms priced positively against their last private valuation, although the first few weeks of public trading have seen some ups and downs. We expect IPOs to sustain the momentum we've seen since the beginning of 2017, especially for companies nearing or over the €1 billion mark. We still see public investors inside and outside of Europe choosing to back large growing businesses, especially businesses with a technology focus. We expect this favorable IPO environment for VC-backed businesses to track the performance of global equity markets, with the potential of market weakness or larger sentiment changes about the risk with technology firms to reduce demand for new listings.

Exit value already at a four-year high

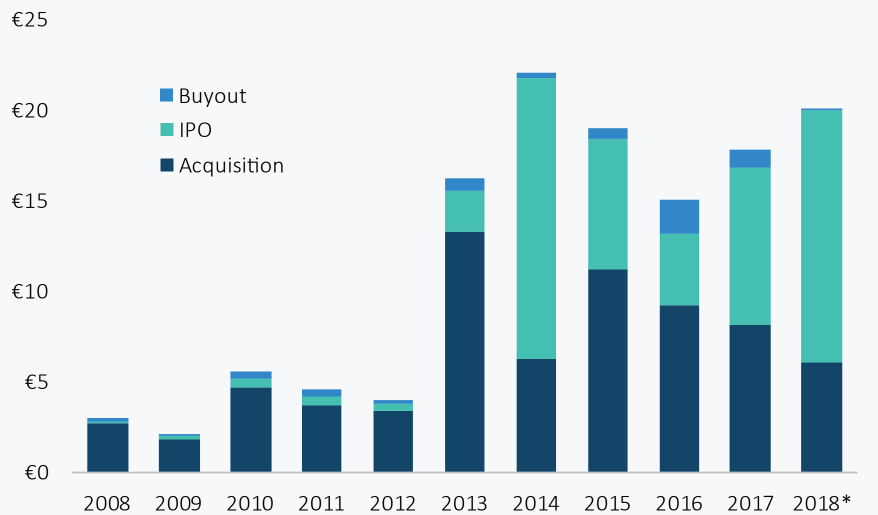
European VC exit activity



Source: PitchBook
*As of September 30, 2018

IPOs account for more than two-thirds of exit value in 2018

European VC exits (€B) by type



Source: PitchBook
*As of September 30, 2018

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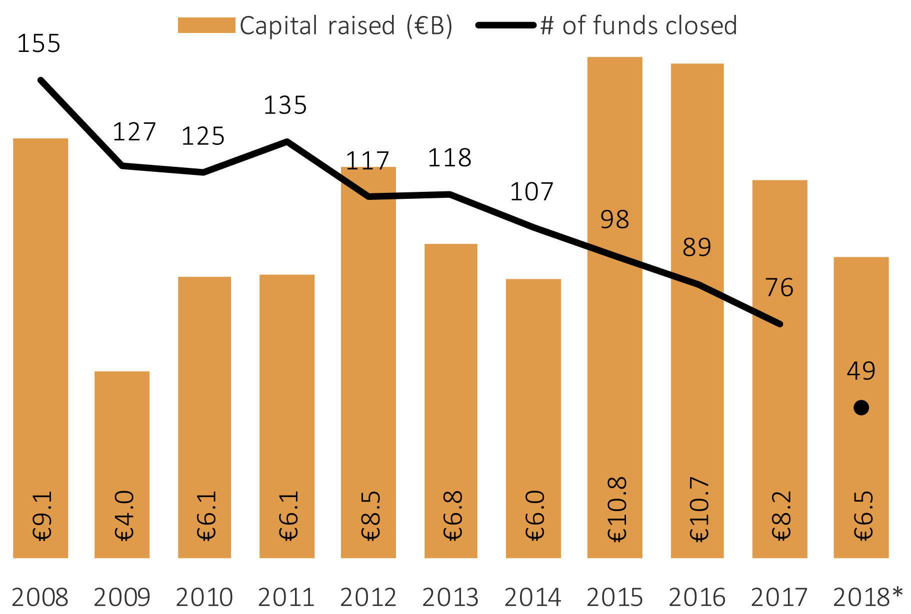
Fundraising

Fundraising was down in the third quarter, with €2.0 billion raised, just shy of the €2.1 billion raised in 2Q. Over the first three quarters, VCs closed on €6.5 billion, putting 2018 on pace to surpass 2017 figures. Using a four-quarter rolling average to account for the inherent lumpiness of fundraising data, we see that capital raised has leveled out over the past six quarters, averaging about €2 billion per quarter. Fund count was depressed for a second straight quarter at just 13 funds closed; 49 funds have been closed in the first three quarters, down from the 59 funds closed in 2017 over the same timeframe. Annual fund count is expected to fall year over year, but elevated levels of capital raised indicates that limited partners (LPs) continue their enthusiasm for the asset class. The fewer, larger funds in recent quarters may signal consolidation of LPs' commitments toward select managers with unique strategies or proven success as venture investors.

Median fund size rose more than 50%, from €79.7 million in 2017 to €123.2 million in 2018. Funds closed in the €100 million to €500 million range now make up 58.1% of funds closed by count, up from 13.2% just six years ago. While startups across Europe previously cited access to late-stage capital as a barrier to development, investors raising larger funds are poised to distribute capital across funding stages. This is in comparison to a decade ago when 75.9% percent of funds were micro-funds (vehicles smaller than €50 million), and very few vehicles existed to fund larger capital raises. Many venture investors are raising larger funds to keep up with the market dynamics of elevated investor competition and a trend toward larger deal sizes. Additionally, recent PitchBook analysis has shown that larger funds have outperformed in the most recent period. The combination of market factors and superior fund performance are likely to exacerbate the trend toward larger funds.

Capital raised stays strong while fund count slides

European VC fundraising activity



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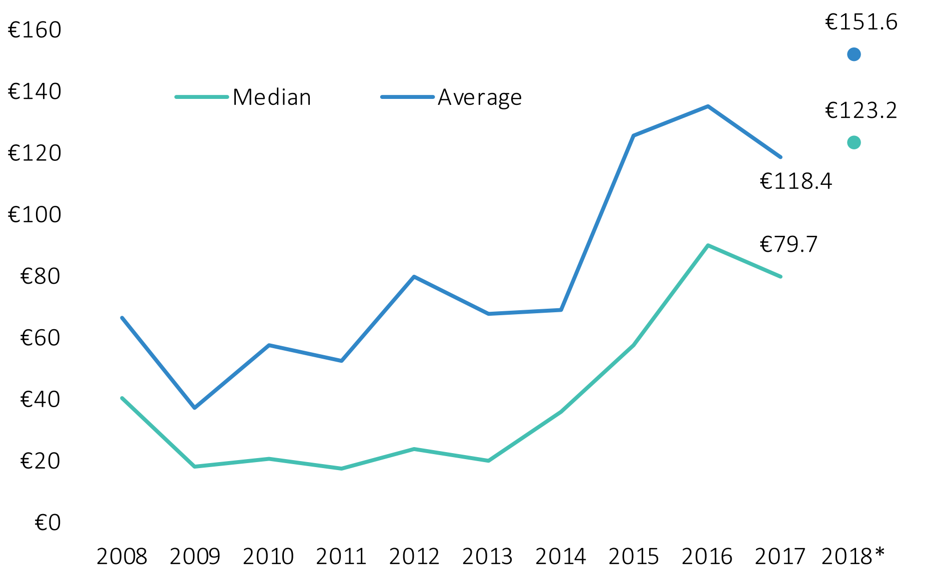
After a blip in 2017, fund sizes are back on the rise

Median and average European VC fund sizes (€M)



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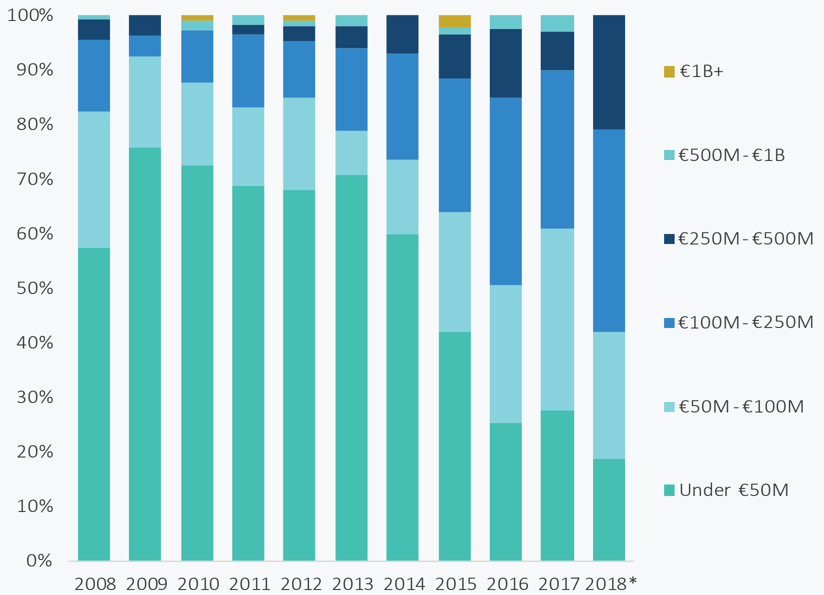
Capital continues to be concentrated in regions with already-developed venture ecosystems. VCs in the UK & Ireland region have attracted the most commitments this year, with €2.4 billion raised across 16 funds. German funds, however, closed on the greatest amount of capital in the third quarter, raising €700.0 million total. The largest fund of the quarter was the inaugural fund of Munich-based Digital+ Partners, which closed on €350.0 million to invest in technology firms in the industrial and finance sectors. The sizable first-time fund boasts backing from the European Investment Fund (EIF) and KfW Group, Germany's development bank. In October, KfW announced the launch of KfW Capital, a €200 million state-backed initiative to back VC and venture debt funds targeting startups in the local ecosystem.

The France & Benelux region has seen the greatest decline in fund count, from a high of 71 funds closed in 2011 to a low of 16 funds in 2017. Despite the comedown, this region continues to attract a significant amount of new funds and capital raised. French VCs closed four funds in 3Q, the most of any European country. The largest French fund closed in 3Q was the €200.0 million Build-up International Fund, managed by Bpifrance, a state-backed investment bank. The fund targeting French companies is looking to expand internationally via buy-and-build strategies and signals momentum from government capital to mobilize local businesses for global growth.

Smaller funds continue to fall out of favor

European VC funds (#) by size



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