

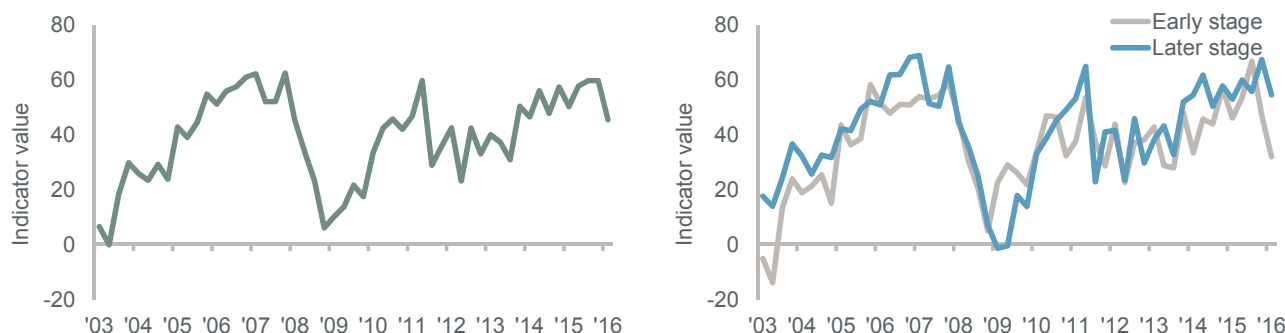
»» Market sentiment drops sharply

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- Gloom spreads to later-stage financiers
- Fundraising climate drops but remains very good
- IPO climate is frosty again

German Private Equity Barometer – business climate



Source: KfW Research, BVK

Depressed Sentiment at the start of the year

Sentiment on the German private equity market cooled significantly at the beginning of the year. The German Private Equity Barometer's business climate index fell 14.3 points to 45.4 balance points in the first quarter of 2016. In contrast with the previous quarter, when strong confidence in the later-stage segment offset the slump in confidence in the early-stage segment, sentiment eroded in both segments of the market. Equity investors are more pessimistic about their current business situation and their expectations for the future. The indicator for the current business situation dropped by 11.3 points to 50.8 balance points, while the indicator for business expectations fell 17.3 points to 40.0 balance points.

Confidence among early-stage financiers drops again

The business climate in the early-stage segment of the German private equity market deteriorated further at the beginning of the year. The business climate indicator in the early-stage segment fell in the first quarter (-15.1 points to 32.0 balance points) and is now below its long-term average. Confidence in the past two quarters took a real nosedive from the record high in the third quarter of 2015. A slump of comparable proportions has only ever been seen once before in the first half of 2008, shortly before the onset of the financial crisis. Early-stage financiers are taking a much dimmer view of both their current business situation and their expectations for the future. The indicator for the current

business situation dropped by 17.0 points to 33.3 balance points, while the indicator for business expectations fell 13.2 points to 30.7 balance points. Unlike in the previous quarter, when the decline in sentiment was not reflected in the assessment of the underlying conditions, some of the climate indicators in the early-stage segment have now deteriorated as well – although most of them not as sharply as the business climate. The fund-raising climate, for example, remains at a very good level despite falling steeply from its record high. The climate for IPOs has worsened as well.

Downturn in sentiment spreads to later-stage financiers

After the later-stage financiers ended the previous year in a positive mood, sentiment has now reversed in this segment as well. The business climate indicator fell by 12.8 points to 54.6 balance points in the first quarter of 2016. In contrast with the early-stage segment, however, the business climate is still good and above the long-term average. Later-stage financiers are also revising downwards their assessments of both their current business situation and their expectations for the future. The indicator for the current business situation dropped 6.5 points to 62.7 balance points, while the indicator for business expectations fell more sharply by 19.1 points to 46.4 balance points. The decline is also reflected by more negative assessments of the climate indicators which nevertheless remained good to very good.

VC market sentiment is surprisingly weak

Confidence among early-stage and later-stage financiers was muted at the beginning of the year – as was the case in the previous year, which eventually brought forth record high levels of business confidence. The business climate in the later-stage segment remains very good despite the decline, but it slipped below its long-term average in the early-stage segment. The early-stage financiers' assessment of the climate for IPOs has worsened along with the business climate. Their assessment of IPO prospects for start-ups is on the lowest level of the last three years. Still: "Sentiment on the market is currently worse than we would expect based on the evaluation of the underlying conditions" said Dr Jörg Zeuner, Chief Economist of KfW Group. "We assume,

however, that the favourable underlying conditions will eventually hold sway and the muted sentiment at present will not make venture capital investors less willing to invest in the long term. We see no reason why this would be the case". Ulrike Hinrichs, Managing Director of the BVK, is also optimistic: "The willingness to invest is there. The experiences of last year have also shown that sentiment can quickly turn positive over the course of the year. Any relaxation in the very high valuations or successful exits would boost sentiment in the sector at a single stroke. The recent announcement by the German Federal Ministry of Finance that no venture capital act will be introduced in the current round of legislation came as a disappointment for our venture capital investors, however. We were all hoping for a real improvement following the many political commitments of recent years." ■

Appendix: Equity market climate in figures

German Private Equity Barometer

Climate indicators		Q1/2003 to Q1/2016		2014			2015				2016
		Max	Ø	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Business climate	Total	62.4	39.2	56.0	47.8	57.4	50.3	57.8	59.7	59.7	45.4
	ES	66.8	36.4	45.7	43.9	56.8	46.1	53.5	66.8	47.1	32.0
	LS	68.9	41.3	61.7	50.4	57.8	52.9	60.0	55.8	67.4	54.6
Market factors:											
Fundraising	Total	58.3	5.4	29.4	34.5	38.5	41.8	38.3	48.1	58.3	38.8
	ES	42.4	-12.0	-2.6	5.8	26.2	11.8	-17.0	13.7	42.4	10.2
	LS	70.0	19.2	52.9	56.8	46.5	61.9	70.0	69.8	69.4	57.4
Acquisition prices	Total	62.7	6.7	-27.1	0.6	-11.9	-27.1	-30.2	-42.7	-27.6	-23.3
	ES	70.9	29.7	9.2	23.8	18.3	-9.6	9.0	-19.8	-4.5	-3.7
	LS	54.5	-10.3	-48.9	-16.0	-30.7	-38.0	-52.3	-55.1	-41.9	-37.1
Exit opportunities	Total	58.6	5.8	41.2	39.5	38.8	50.7	57.2	58.6	52.5	38.1
	ES	46.0	-5.7	21.1	17.6	32.3	23.0	35.1	28.1	26.0	13.0
	LS	74.5	13.9	52.3	54.2	42.9	66.5	68.2	74.5	68.1	55.3
Demand	Total	63.6	45.4	41.1	44.2	42.9	34.3	35.9	49.8	45.8	38.8
	ES	75.8	51.8	55.9	58.9	73.2	51.4	48.6	58.8	66.2	55.9
	LS	65.9	41.7	32.6	34.2	24.0	22.8	29.0	44.6	33.2	26.8
Demand quality	Total	41.4	26.1	23.2	24.9	14.9	17.2	23.7	26.5	23.4	31.1
	ES	63.8	33.6	30.7	25.0	29.7	29.8	27.1	25.8	37.9	35.9
	LS	43.2	20.7	19.0	24.8	5.4	8.8	21.7	26.9	14.5	27.9

Comments and Abbreviations:

Differences to previous publications are due to extrapolation.

E(arly)S(tage)

L(ater)S(tage)

Source: KfW Research, BVK

Calculation of the German Private Equity Barometer:

The German Private Equity Barometer is based on a quarterly survey of the 200+ members of the German Private Equity and Venture Capital Association (Bundesverband Deutscher Kapitalbeteiligungsgesellschaften – BVK). The German Private Equity Barometer reports the business climate in the German private equity capital market. The business climate is calculated as the mean of the net balance of the weighted assessments of the current business situation (positive responses minus negative responses, expressed as a percentage) and the equivalent net business expectations for the coming six months. The responses provided by interviewees are weighted to reflect the volume of capital under management and the investment focus of all BVK members.