

»» German private equity market starts the year on a positive note

14 May 2018

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- VC investors are becoming more cautious
- Price climate in the later-stage segment is still in a trough
- Expectations remain less positive than business climate

Business climate in the German private equity market is improving again

The German private equity market started the year on a high note. The business climate index of the German Private Equity Barometer rose by 2.4 points to 66.7 balance points in the first quarter of 2018. Both the business situation and expectations were slightly better than in the previous quarter. The indicator for the current business situation rose to 71.2 balance points (+2.1), while the indicator for business expectations climbed to 62.1 balance points (+2.5).

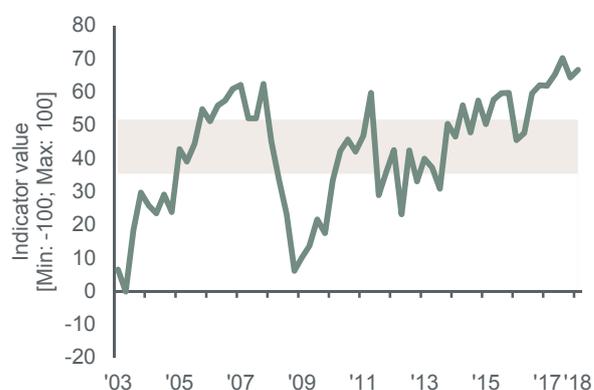
The business climate indicator and most of the other indicators remained very stable at the beginning of the year. Assessments of the level and quality of deal flow and the exit and support environment changed only marginally. The fundraising and innovation climates fell slightly but their general upward trend remains intact.

VC investors' reluctance is growing

The business climate in the venture capital market cooled off again slightly at the start of the year. The business climate indicator for the early-stage segment dropped by 3.3 points to 63.0 balance points in the first quarter of 2018 as a result of falling business expectations. The indicator for the current business situation thus climbed to an all-time high of 67.7 balance points (+0.4), while the indicator for business expectations dropped by 7.1 points to 58.2 balance points. Relative to their business situation, equity providers had the lowest expectations of the past three years.

The reason for the more subdued business expectations may have been the increased pressure on write-downs in the VC area at the beginning of the year. The other indicators, at least, are emitting rather positive signals. The fundraising and exit climates remain very good. Dissatisfaction over entry prices is also down from its peak. Assessments of the level and quality of deal flow have also increased.

Business climate indicator – overall market



Note: The grey shaded area shows the normal range defined on the basis of historic indicator values.

Sources: KfW Research, BVK.

Business climate indicator – early-stage market



Note: The grey shaded area shows the normal range defined on the basis of historic indicator values.

Sources: KfW Research, BVK.

Dissatisfaction of later-stage investors over entry prices remains high

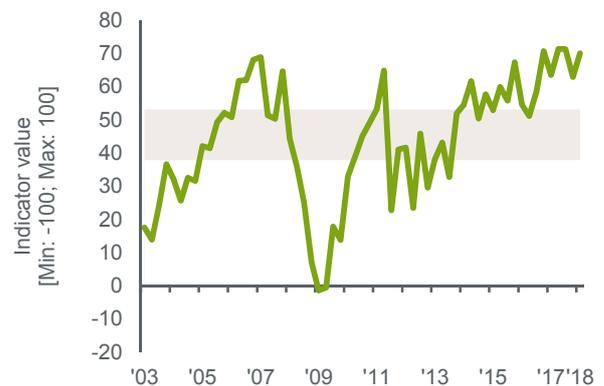
The business climate in the later-stage segment of the German private equity market recovered at the start of the year from its previous decline. The business climate indicator gained 7.1 points in the first quarter of 2018, reaching 70.0 balance points. Equity providers assessed both the business situation and expectations more positively than in the previous quarter. The indicator for the current business situation rose by 4.1 points to 74.5 balance points, while the indicator for business expectations increased by 10.1 points to 65.6 balance points.

The market environment in the later-stage segment hardly changed at the beginning of 2018. Later-stage investors rated the fundraising climate, exit environment, pressure on write-downs and innovation climate very positively. After improving slightly in the previous quarter, however, their assessments of the quantity and quality of deal flow and entry prices were down slightly again. Dissatisfaction with entry valuations ascertained remains near peak levels.

Successful start to the new year – but expectations are still less positive than the business situation

German private equity investors carried their optimism from the end of last year over into the new year. The business climate remains very good. Equity investors are particularly pleased with the business situation but their expectations are less positive. However, expectations have been less positive than the business situation for 13 consecutive quarters now, even though the business climate during this time has improved significantly. Investors thus appear to be somewhat suspicious of the positive market development. One likely reason is the low-interest environment, the end of which is wrapped in uncertainty. Should anything change here, it will have ramifications for key conditions such as entry valuations, fundraising or exit opportunities. Equity investors are thus likely to be cautious in assessing their business expectations.

Business climate indicator – later-stage market



Note: The grey shaded area shows the normal range defined on the basis of historic indicator values.

Sources: KfW Research, BVK.

“Short-term interest rates in Europe will remain at record low levels for the foreseeable future,” said Dr Jörg Zeuner, Chief Economist of KfW Group. “We therefore expect continuing good conditions for fundraising and exits. We are on the way to significantly improving our supply of venture capital to start-ups in Germany at every stage of their business. I am pleased that this market environment is helping us.”

Ulrike Hinrichs, Managing Director of the German Private Equity and Venture Capital Association (BVK), added: “The continuing positive underlying sentiment is good for the market and the economy. A stable private equity market in particular is best able to perform its task: that of providing start-ups and SMEs with private equity. The indications of subdued expectations, on the other hand, reflect the general uncertainty over how long the low-interest environment and the unusually long cyclical upswing in Europe will continue. At the moment, however, there is no end in sight.” ■

Annex: Sentiment on the German private equity market in figures**German Private Equity Barometer**

Differences to previous publications are due to extrapolation.

Sentiment indicators		Q1/2003 to Q1/2018		2016			2017				2018
		Max	Avg.	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Business climate	Total	70.2	42.2	47.6	59.6	62.1	61.9	65.2	70.2	64.3	66.7
	Early	69.0	39.3	41.3	61.1	48.3	59.7	56.3	69.0	66.3	63.0
	Later	71.4	44.4	51.2	58.7	70.7	63.5	71.4	71.3	62.9	70.0
Market climate											
Fundraising	Total	79.2	12.6	40.3	55.4	59.9	61.8	56.2	60.9	79.2	67.0
	Early	74.9	-4.2	10.2	39.7	38.0	44.4	58.4	48.8	74.9	61.3
	Later	82.4	26.0	59.2	65.6	76.9	80.4	54.4	73.8	82.4	73.3
Entry prices	Total	62.7	0.2	-32.8	-32.9	-38.3	-29.1	-45.5	-43.7	-49.3	-43.2
	Early	70.9	23.9	0.1	1.4	-13.7	7.8	-27.2	-15.5	-27.7	-19.4
	Later	54.5	-17.2	-52.1	-53.3	-54.0	-57.6	-58.2	-67.4	-64.9	-66.4
Exit opportunities	Total	72.0	12.3	50.0	43.4	53.9	49.3	51.6	72.0	60.3	59.4
	Early	59.8	0.1	14.4	27.4	27.2	35.4	33.7	59.8	51.3	56.7
	Later	80.8	20.7	69.2	55.8	70.2	59.6	63.6	80.8	67.0	62.0
Level of demand	Total	63.6	45.6	39.0	45.1	35.7	46.6	44.4	51.0	56.9	57.1
	Early	84.9	54.7	78.2	77.5	73.6	84.9	61.3	63.5	72.1	78.5
	Later	65.9	40.0	15.9	25.6	11.8	17.6	32.8	40.4	45.6	37.5
Quality of demand	Total	41.4	26.2	22.4	10.4	33.0	25.5	30.3	32.0	29.4	28.5
	Early	63.8	32.8	19.2	30.1	41.5	43.7	17.3	24.5	19.9	27.8
	Later	43.2	21.3	24.2	-1.7	27.5	12.0	39.2	38.0	36.2	29.1

Sources: KfW Research, BVK.

Calculation of the German Private Equity Barometer

The German Private Equity Barometer is based on a quarterly survey which the German Private Equity and Venture Capital Association (Bundesverband Deutscher Kapitalbeteiligungsgesellschaften – BVK) conducts among its roughly 250 members and further German private equity companies. 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 the market.