

»» Business confidence continues to break records

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- VC business climate hits new all-time high
- Assessment of exit opportunities clearly above record level
- Later stage: dissatisfaction with entry prices rises for the sixth consecutive quarter

Business climate index breaks through 70-point mark for the first time ever

Sentiment on the German private equity market improved once again in the third quarter. The business climate index of the German Private Equity Barometer increased by 4.9 points to 70.2 balance points in the third quarter of 2017, clearly beating its own record of the second quarter. The indicator for the current business situation rose by 1.9 points to 70.5 balance points, while the indicator for business expectations climbed by 8 points to 69.8 balance points. The trend shows new record high confidence in the early-stage segment of the private equity market. The business climate in the later-stage segment remained very good, virtually unchanged just under the record high of the second quarter.

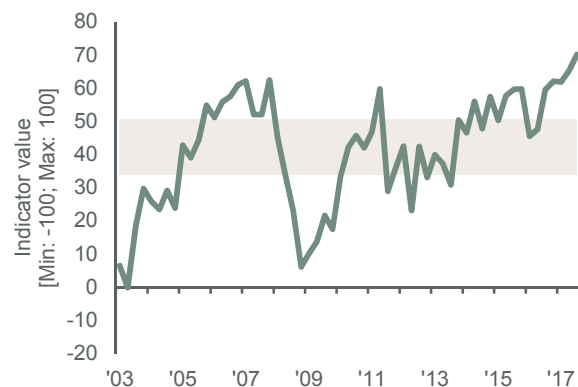
The renewed improvement in the business climate has come about on the back of a much better exit environment. The assessment of exit possibilities was noticeably better than the previous record high of the first quarter of 2015.

VC business climate hits new record high

The business climate in the venture capital market has reached a new record high. The business climate indicator of the early-stage segment rose by 12.8 points to 69.1 balance points in the third quarter of 2017. Both the current business situation and expectations improved significantly. The indicator for the current business situation rose by 9.1 points to 66.7 balance points, while the indicator for business expectations literally soared by 16.5 points to 71.5 balance points.

The VC business climate is being fuelled by positive developments in the market environment. VC investors' assessments of exit and support opportunities rose to new record high levels in the third quarter. The fundraising and innovation climate has also remained very good. Moreover, assessments of the level and quality of deal flows and entry prices have stabilised on their respective levels after slipping in the previous quarter.

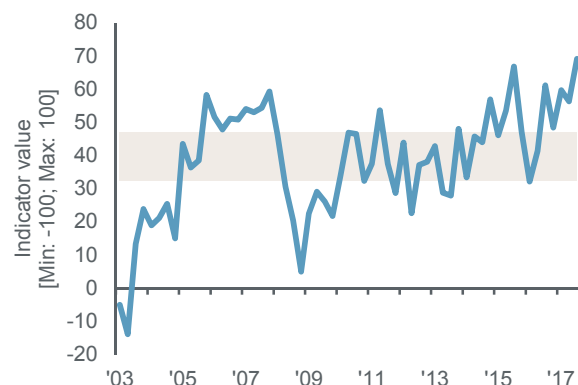
Business climate indicator – overall market



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.

Later-stage investors are still in high spirits

The business climate in the later-stage segment remained exceptionally good. The business climate indicator in the third quarter of 2017 was just under its record high of the previous quarter, at 71.1 balance points (-0.4 points). Investors rated their current business situation marginally less favourable than in the second quarter, but their business expectations are somewhat more positive. The indicator for the current business situation dropped by 2.6 points to 73.7 balance points, while the indicator for business expectations has improved by 1.8 points to 68.5 balance points.

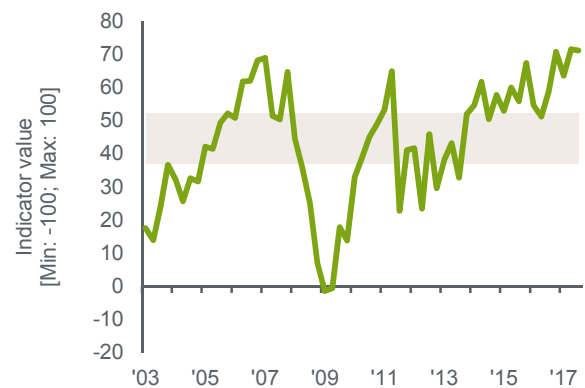
The still very good business climate in the later-stage segment is being sustained by nearly the entire market environment. After dropping in the previous quarter, the fundraising climate is back to just under the record high, while assessments of the level and quality of deal flows have clearly rebounded from their lows and the exit climate is better than ever. Assessments of exit opportunities via trade sales, secondary offerings or buybacks have improved to new record levels. Accordingly, pressure on write-downs has decreased again after a slightly tense first half year. Entry prices remain problematic. Investors' dissatisfaction with the valuations ascertained has risen for the sixth consecutive quarter.

Business confidence is rising steadily

Sentiment in the German private equity market is currently outstanding. The fundraising and exit climate, in particular, is exceptionally good. Just a few years ago, many exits could not be realised as expected – one of the reasons equity providers were hardly willing to invest in venture capital. That had a very adverse impact on the German private equity market. The VC segment suffered most under the market environment. Because of the uncertainty surrounding fundraising, VC investors were also reluctant to make larger sums available to start-ups – placing these at a significant disadvantage compared with their international competitors, especially in the USA. Depending on the financing stage, US VC investors made five to nine times more capital available to their enterprises.

‘The exceptionally good fundraising climate has now reached start-ups as well’, said Dr Jörg Zeuner, Chief Economist of KfW Group. ‘Funding rounds are getting bigger. The latest figures from the German Private Equity and Venture Capital Association illustrate that more than twice as much was invested per start-up in the past two half years than in 2012

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.

and before. The higher funding rounds are necessary to prevent domestic start-ups from falling behind their international competitors from the start. The situation still takes some getting used to for local VC investors, as we can see from their dissatisfaction with entry prices.’

Ulrike Hinrichs, Managing Director of the German Private Equity and Venture Capital Association (BVK), added: ‘What is particularly pleasing is that the very good mood and positive outlook on the future has now arrived in the VC segment as well. All stakeholders made great progress in the past years to move Germany forward in start-up funding. Looking at the generally high valuation level, we must admit that, thanks to Draghi’s special boost, the overall economic conditions, the low interest rate level but also the strong business results are contributing to these company valuations. However, this is not specific to private equity or venture capital, if we take a look at German and international stock market indexes, which have been smashing records these days.’ ■

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 Q3/2017		2015	2016				2017		
		Max	Avg.	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3
Business climate	Total	70.2	41.4	59.7	45.5	47.6	59.6	62.1	61.8	65.2	70.2
	Early	69.1	38.4	47.1	32.1	41.3	61.1	48.3	59.7	56.3	69.1
	Later	71.5	43.7	67.4	54.5	51.2	58.7	70.7	63.5	71.5	71.1
Market climate											
Fundraising	Total	61.5	10.5	58.3	39.1	40.3	55.4	59.9	61.5	56.1	60.7
	Early	58.4	-6.7	42.4	10.3	10.2	39.7	38.0	44.3	58.4	48.7
	Later	80.2	24.2	69.4	57.7	59.2	65.6	76.9	80.2	54.2	73.8
Entry prices	Total	62.7	1.9	-27.6	-23.8	-32.8	-32.9	-38.3	-28.9	-45.4	-43.4
	Early	70.9	25.6	-4.5	-3.9	0.1	1.4	-13.7	7.9	-27.2	-15.4
	Later	54.5	-15.4	-41.9	-37.7	-52.1	-53.3	-54.0	-57.6	-58.2	-67.2
Exit opportunities	Total	71.9	10.6	52.5	38.5	50.0	43.4	53.9	49.3	51.6	71.9
	Early	60.0	-1.8	26.0	13.1	14.4	27.4	27.2	35.4	33.8	60.0
	Later	80.8	19.3	68.1	55.6	69.2	55.8	70.2	59.8	63.7	80.8
Level of demand	Total	63.6	45.3	45.8	38.7	39.0	45.1	35.7	46.8	44.4	51.0
	Early	85.0	54.0	66.2	56.2	78.2	77.5	73.6	85.0	61.3	63.5
	Later	65.9	39.9	33.2	26.6	15.9	25.6	11.8	17.7	32.7	40.3
Quality of demand	Total	41.4	26.1	23.4	30.9	22.4	10.4	33.0	25.6	30.2	32.0
	Early	63.8	33.1	37.9	36.0	19.2	30.1	41.5	43.8	17.3	24.6
	Later	43.2	21.0	14.5	27.6	24.2	-1.7	27.5	12.0	39.2	38.0

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.