

VC market off to a good start in 2021

– Sentiment continues to rise

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- Assessments of sentiment indicators for fundraising, appetite for new investment and exits improved greatly
- Deal flow quality and quantity marginally below all-time highs
- Investors again significantly more dissatisfied with entry valuations

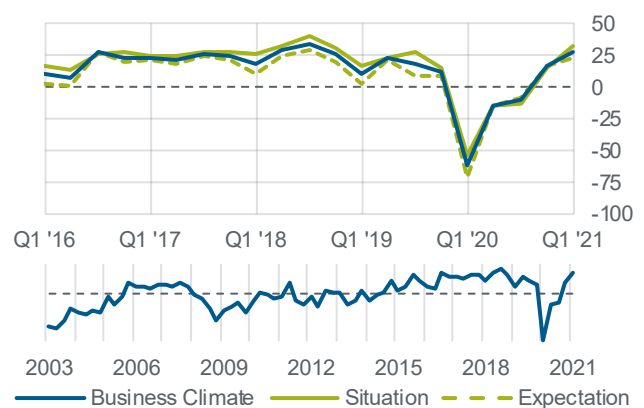
VC sentiment builds on positive trend

The positive development of VC business sentiment has continued into the new year. In the first quarter of 2021 the sentiment indicator of the early-stage segment rose by 11.5 points to 27.8 balance points. Assessments of the current business situation improved much more strongly than expectations. The indicator for the current business situation rose by 16.4 points to 31.9 balance points, while the indicator for business expectations increased by 6.5 points to 23.7 balance points. With this rise the indicator moved very close to its previous all-time high of 34.5 balance points, which it reached in the third quarter of 2018.

Market environment better than at any time since 2018

Only a year after the coronavirus-induced downturn in sentiment, nearly all sentiment indicators for the market environment have turned positive – many closing in on their all-time highs. Assessments of fundraising and exit opportunities improved particularly strongly in the first quarter of 2021. The fundraising climate has probably benefited from the implementation of the future fund and investors' growing interest in alternative forms of investment such as venture capital. A further reason that is likely to have influenced the strong improvement in assessments of exit opportunities is the arrival of the US SPAC boom in Europe. Mergers with special purpose acquisition companies ('SPACs') are not a new exit variant but are meeting with growing endorsement. Whether SPACs will be available as an exit variant in the long term remains to be seen, however. The strong development in fundraising and exits also appears to have increased appetite for new investments. Their assessments have climbed to a new high – no doubt also because of the quality and strength of VC deal flow, the assessments of which have also risen to near all-time high levels. The high uncertainty about how severely the crisis affected start-ups weighed on entry valuations at the beginning of the pandemic. As many digital start-ups are likely to be among the winners of the crisis, however, investors gave the recently rising entry valuations increasingly lower scores.

Development of VC business climate indicator



Sources: KfW Research and BVK.

Key data of VC sentiment indicators

Values in balance points

	Q1/21	Δ vs. Q4/20	High	Low
Business climate	● +27.8	▲ +11.5	▶ +34.5	▶ -61.8
Business situation	● +31.9	▲ +16.4	▶ +39.9	▶ -57.3
Business expectations	● +23.7	▲ +6.5	▶ +29.0	▶ -70.4
Fundraising	● +67.2	▲ +44.0	▶ +69.9	▶ -68.0
Entry evaluations	● -21.3	▼ -23.1	▶ +49.2	▶ -51.0
Exit opportunities	● +49.5	▲ +48.7	▶ +52.4	▶ -74.6
New investments	● +33.0	▲ +26.2	▶ +33.0	▶ -70.6
Dealflow quantity	● +28.4	▲ +6.7	▶ +28.9	▶ -42.7
Dealflow quality	● +25.9	▲ +5.1	▶ +26.5	▶ -21.2
Funding	● +37.2	➡ -1.4	▶ +38.6	▶ -56.9
Taxation framework	● +1.5	▼ -17.1	▶ +36.7	▶ -26.8
Innovation	● +30.2	▲ +19.7	▶ +37.9	▶ -46.0
Write-downs	● +12.5	▲ +18.0	▶ +28.6	▶ -49.7

The colour coding of the balances and the variations is based on the historical values of the respective indicator (1st tercile 'red', 2nd tercile 'amber' and 3rd tercile 'green'). Indicator design may lead to deviations from previous publications.

Sources: KfW Research and BVK.

KfW Research

German Venture Capital Barometer 1st quarter 2021

Comments on the current trend

'The upturn in sentiment in the VC market which we were able to observe at the end of the year 2020 continued in the first quarter of 2021', said Dr Fritz Köhler-Geib, Chief Economist of KfW. 'VC investors' very good assessments of deal flow is particularly pleasing. After all, promising deal flow lays the foundation for promising VC investments. The indicators for deal flow quality and quantity are marginally below their all-time highs. This might reflect the fact that the coronavirus crisis accelerated demand for many start-ups because it has brought to light the needs for their innovative solutions. This opens up investment opportunities.'

'The rapid return of general market sentiment and the most important indicators to their historic all-time highs shows that venture capitalists and start-ups have finally left the coronavirus pandemic behind and are looking to the future', said Ulrike Hinrichs, Managing Director of the German Private Equity and Venture Capital Association (BVK). 'What is encouraging are the more optimistic assessments of fundraising conditions and the exit environment, which has long been eyed very critically. Rising valuations promise attractive sales prices. The stock exchange is again being seen as a realistic exit option thanks to a growing IPO pipeline and the SPAC debate. It is not surprising that venture capitalists are significantly more critical of the tax environment. With the Fund Location Act, the German Federal Government fell short of expectations and missed a great opportunity to introduce internationally competitive regulations both in the field of employee participation in start-ups and in the taxation of turnover of fund management services.'

Calculation of the German Venture Capital Barometer

The German Venture Capital Barometer is based on a quarterly survey of the approx. 200 members of the German Private Equity and Venture Capital Association (Bundesverband Deutscher Kapitalbeteiligungsgesellschaften – BVK) and further German private equity companies. The German Venture Capital Barometer has been published as a separate sentiment indicator for the German venture capital market since the second quarter of 2019. It was previously part of the German Private Equity Barometer, the sentiment barometer for the overall private equity market in Germany. It reports the business climate in the German venture capital market on the basis of assessments provided by private equity firms with a focus on investments in start-ups and young technology companies. All sentiment indicators represent the average of the balance of situation assessments (share of 'good' minus share of 'bad') and the balance of expectations identified at the same time for the coming six months, adjusted by their respective historical mean value.