

VC business sentiment drops although situation has improved again

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- VC fundraising climate makes renewed attempt to match record
- VC investors' dissatisfaction with deal flow quality drops significantly
- IPO climate has plunged

More pessimistic expectations drag VC sentiment down

The business climate in the German venture capital market has dropped. The early-stage segment indicator fell by 6.1 points to 16.8 balance points in the third quarter of 2019. VC investors rated their current business situation more positively again but pessimism around their expectations returned. The indicator for the current business situation rose to 26.5 balance points (+2.7), while the indicator for business expectations fell sharply to 7.1 balance points (-14.8).

In alignment with the autumn season, amber and red have increasingly become the dominant colours on the VC sentiment indicators. Nonetheless, some dots remained green, such as the fundraising climate, which surged. After a weaker second quarter, it is making a renewed attempt to match its previous record. The write-off situation and the innovation climate both developed positively and can be regarded as good. But the exit climate, which had just recovered over the summer after its slump in the first quarter, plunged and just slipped into negative territory again for the first time since early 2014. What is setting the pace is the IPO climate, which deteriorated massively, presumably as a result of unfulfilled expectations about major start-up IPOs in the US in the past quarters. At the same time, IPOs of start-ups in Germany continue to be in short supply. There are different developments with respect to the deal flow climate, which dropped slightly in the second quarter. Whereas assessments of VC deal flow amounts are now improving again slightly, satisfaction with its quality dropped massively and is now just a notch above the previous low. This quality assessment may have to do with entry valuations of entrepreneurs seeking VC, which are being seen as exaggerated. Assessments of entry prices thus plunged to a new low.

Development of VC business climate indicator



Source: KfW Research and BVK.

Key data of VC sentiment indicators

Values in balance points

	Q3/19	Δ vs. Q2/19	High	Low
Business climate	● +16.8	↓ -6.1	▲ +34.3	▼ -50.6
Business situation	● +26.5	↑ +2.7	▲ +39.9	▼ -59.5
Business expectations	● +7.1	↓ -14.8	▲ +28.6	▼ -44.7
Fundraising climate	● +68.9	↑ +11.9	▲ +71.6	▼ -66.3
Entry prices	● -47.6	↓ -15.8	▲ +48.9	▼ -51.3
Exit opportunities	● -2.5	↓ -36.0	▲ +51.4	▼ -75.6
including: IPOs	● -19.2	↓ -23.7	▲ +76.9	▼ -53.5
Dealflow quantity	● +12.0	↑ +6.1	▲ +29.2	▼ -42.6
Dealflow quality	● -21.3	↓ -17.2	▲ +27.1	▼ -22.2
Taxation framework	● +10.7	↓ -3.9	▲ +39.1	▼ -25.4
Innovation climate	● +21.0	↑ +10.7	▲ +38.7	▼ -44.7
Write-down pressure	● +12.6	↑ +2.1	▲ +27.9	▼ -38.5

The colour coding of the balances 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.

Source: KfW Research and BVK.

KfW Research

German Venture Capital Barometer: 3rd quarter 2019

Commentary on the current development

‘Currently, there is no clear trend in the development of business sentiment in the German venture capital market’, said Dr Georg Metzger of KfW Research. ‘On the one hand, business expectations and the market environment have deteriorated. On the other hand, the actual business situation still presents itself very positively. Moreover, the fundraising climate has reached increasingly higher and unprecedented levels for the past three years. What direction market sentiment will ultimately take will presumably depend on how the market reacts to the shock from the events surrounding WeWork. Start-ups in search of VC can help to overcome investors’ scepticism by convincing them more than ever of their quality.’

Commenting on the deal flow aspect, Ulrike Hinrichs, Managing Director of the German Private Equity and Venture Capital Association (BVK), added: ‘The steady, positive sentiment and strong demand for venture capital will likely form the basis for another strong venture capital year. Venture capital tops the list as the preferred form of finance of a growing number of ambitious entrepreneurs. For venture capitalists, this means identifying the relevant and most attractive ones from among the multitude of investment applications. The exit side remains challenging. Successes here would significantly improve sentiment.’

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.