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2024 US Venture Capital Outlook: Midyear Update

Checking in on our 2024 US VC predictions

PitchBook is a Morningstar company providing the most comprehensive, most accurate, and hard-to-find data for professionals doing business in the private markets.

2024 outlooks

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Introduction

At the end of every year, we share our views on how the year ahead will unfold for US venture capital. We offered seven outlooks for 2024, and it is time to take stock of those trends to see how they are tracking. We look forward to sharing our takes on these and other developments throughout the year in our quarterly reports, which include the PitchBook-NVCA Venture Monitor and the US VC Valuations Report.

Expectations for the turnaround in the VC market entering 2024 were not especially high. The headwinds that triggered the market slowdown were well entrenched in the economy, and balance had not been found to offset the heightened risks. Through the first six months of 2024, inflation continued to be sticky, interest rates remained at the high level they ended 2023 with, and geopolitical events kept a haze on the horizon.

Venture has unsurprisingly been slow. Overall exits have been poor, despite several high-visibility IPOs. Fundraising had one of the slowest quarters since 2017 in Q1, and Q2 has been a struggle even though several name-brand VCs raised billions of dollars. Dealmaking has leaned heavily on AI, which continues to make headlines with high valuations and large deals.

There does seem to be a higher degree of desperation from the market. With more than 55,000 companies currently VC-backed, many companies are facing last-ditch options for continuing growth and development. Many of the M&A exit transactions we have collected in 2024 are small, even to the size that transaction values have gone unreported. Down rounds continue to pick up as well, as companies concede with investors to secure funding.

Venture market resets take time. Valuations remain relatively high, especially for AI companies, and the aggregate value of unicorns is higher than ever. However, one of the consequences of the slowdown now adding excessive pressure to the market is the lack of returns. Our data shows that the rate of distributions back to LPs is at its lowest since 2009. The market is exponentially larger than it was back then, making the exposure of the LP community to VC that much higher. With fewer returns and less capital to recycle into the market, the full impact of the slowdown may still be ahead.

Our outlooks for the year centered on themes that had driven the narratives across the venture landscape. With our midyear update, the analysis is not solely about how our outlooks have fared to date, but also a forward-looking examination of the market and what could happen next within these themes.

Our other outlook reports from December 2023 include US PE, European Private Capital, Healthcare, Consumer Technology, Allocator, Industrial Technology, and Enterprise Technology.

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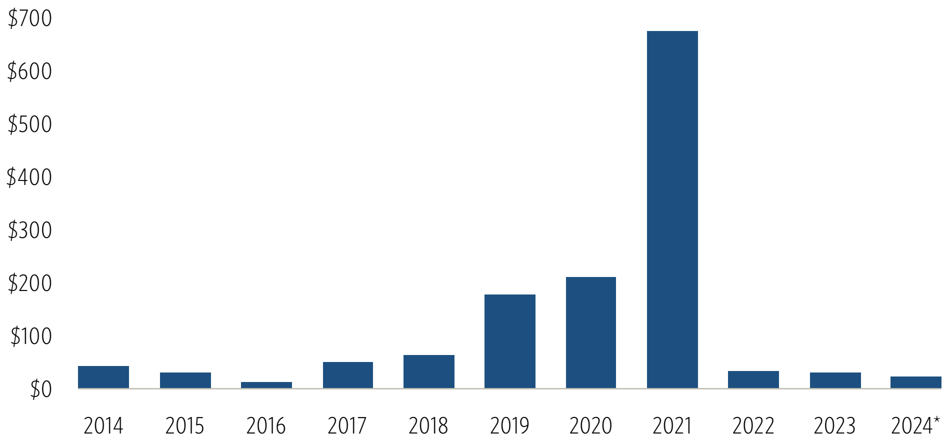
Outlook: Positive economic signals through 2023 will spur a comeback in IPOs in 2024.

VC public listing exit value ($B)



Source: PitchBook • Geography: US • *As of May 23, 2024

Rationale from December 2023

Forecasting the precise moment when the IPO market will reopen is a very nuanced task, yet as we approach the end of 2023, we are observing encouraging indicators that could point to a resurgence in the upcoming year. Through the third quarter of 2023, the US economy has been performing better than expected. GDP increased 5.2% in Q3—up from 2.1% in Q2—further calming expectations that the economy will fall into a recession. Moreover, the federal reserve (the Fed) has yet to raise rates since July 2023, reinforcing expectations that the central bank has concluded its current cycle of rate hikes.

Continued slowed inflation is even more likely, given that many supply chain bottlenecks brought about by the global COVID-19 pandemic appear to be largely resolved. There exists a correlation between supply chains and inflation, as evidenced in the Global Supply Chain Pressure Index; as of October 2023, the index has fallen significantly from its highest-ever peak in December 2021.[1]

Market volatility is also on a downward trend, as reflected in the Cboe Volatility Index (VIX), commonly known as Wall Street's fear gauge. Presently, the VIX stands at around 13, below its long-term median of 18 and significantly lower than the peaks witnessed over the past 18 months—like the 37.52 recorded in March 2022. On the investor side, lower volatility reduces the perceived risks associated with IPO investments by minimizing concerns about sudden and adverse market swings, thus potentially encouraging even more participation.

1: "Issue Brief: Supply Chain Resilience," The White House, November 30, 2023.

Midyear update

It would be difficult to say the IPO market has reopened or even to call the activity in H1 a slight opening of a window. Yes, four large tech IPOs were completed for about $17 billion in exit value, but four is a small number. Just 22 companies have completed IPOs through May (at the time of writing), so the big question to answer is "why?"

To start, inflation has remained above the Fed's 2% target. This has tanked the idea of a high number of rate cuts this year that would, theoretically, boost the market. Now, the expectation for the number of cuts has lowered and been pushed back. The May Consumer Price Index figure came in at 3.3% YoY and has remained within the 3% to 4% range for 10 months. On top of the high rates and inflation, the US economy slowed during the first quarter of 2024 to an annualized pace of 1.3%. The positive economic signs from the end of 2023 have been decidedly less positive than anticipated in 2024 from an IPO rebound perspective.

There are other factors to consider for the subdued IPO market. If strong public market performance is supposed to be a driver of VC-backed IPOs, the divided markets have not been enticing to private companies. In general, megacaps continue to drive returns. The NASDAQ 100 is up more than 18% on the year, but equal weighted, it is up around 5%. The small-cap Russell 2000 Index is only up just over 1.0%.

Those four tech companies have performed well post-IPO, but there has been little movement toward further listings since Ibotta's in April. Private markets continue to struggle through the high multiples the markets placed on revenues and growth a few years ago. As those multiples have declined in the public markets, the ability to command positive valuation growth—at least to the desired degree—is challenging. Companies in strong capital positions can make IPO decisions that best fit their needs. Stripe has raised billions over the past year to buy back shares of existing investors and employees, providing liquidity to those in need and extending the company's timeline to its future IPO.

Market uncertainty is not likely to dissipate quickly, adding risk to potential listings throughout the rest of the year. The market has been intent in its attention to inflation figures (which remain elevated globally), central bank rates (the European Central Bank was the first central bank to make a cut), and geopolitical tensions that could spiral into market volatility if not tended to properly. The outlook for IPOs over the second half of the year is not sterling. While there should be several more name-brand listings, the likelihood of a surge in listings is low.

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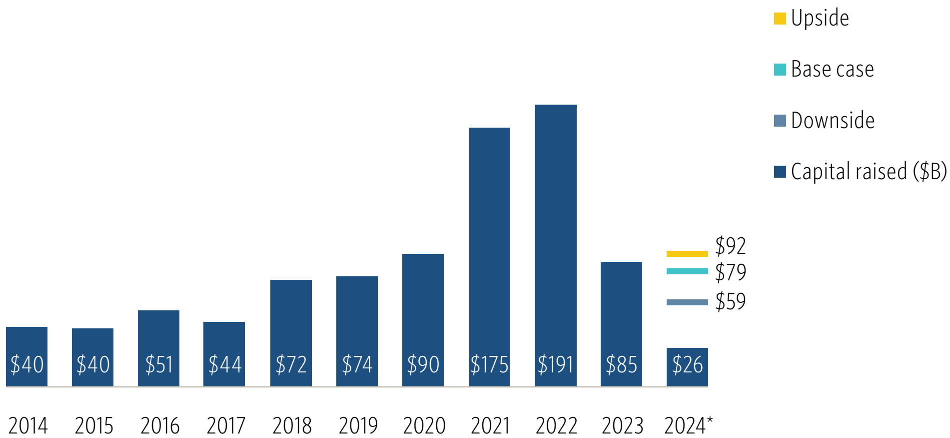
Outlook: US VC fundraising is expected to increase, making it stronger than 2023 but comparable with 2020 figures.

VC capital raised ($B) with 2024 estimates



Source: PitchBook • Geography: US • *As of May 23, 2024
Note: Forecasted figures are as of full-year 2024.

Rationale from December 2023

With the exit environment remaining largely closed in 2023, the rate at which capital is being distributed, as a portion of fund net asset value, is at the lowest level since 2003. One of the major reasons for the poor distribution has been a lack of tech IPOs. Public listings generated above 15.4% of the yearly public exits in 2021 but dropped to 5.8% and 8.4% in 2022 and 2023 YTD, respectively, as public market investors have shied away from riskier tech bets. Even as GPs have scrambled to find alternative methods to return capital to LPs, the downturn in distribution rate since Q3 2022 has dropped to a decade-low in Q3 2023.

Lack of liquidity contributes to how much capital can be recycled into new VC funds. During periods of liquidity crunch and economic uncertainty, LPs are more inclined to invest their capital in less risky asset classes to maintain flexibility and respond to changing financial conditions. We estimated a slight increase in total fundraising, comparable with 2020 figures using a time series model to estimate the impact of trailing 12-month distributions on future fundraising efforts. Fundraising figures for the upcoming four quarters ending in Q3 2024 should look similar to annual 2020 US VC trends.

Midyear update

Distribution and exit rates have remained sluggish into 2024. The liquidity crunch continues to pressure fundraising, with $26.1 billion raised across approximately 181 US VC funds as of when data was pulled for this report, making it approximately 30% of the total fundraising value in 2023. Initially, our outlook used 2020 and 2023 as benchmarks, expecting 2024 fundraising to increase over 2023 figures but be comparable with 2020. However, due to a lag in data collection, we have since revised the total 2023 fundraising from the $67.0 billion pulled before year-end 2023 to $84.7 billion. This adjustment has revised our expectations for 2024 fundraising, as 2020 and 2023 figures are now comparable at $84.7 billion and $89.9 billion, respectively.

Currently, we are tracking around $20.4 billion in open funds that have already deployed capital into the VC market. If we extrapolate the current fundraising trends and account for the lags in data collection, the estimated $46 billion in closed and open funds is projected to surpass $67.0 billion. In our original outlook, we produced one forecast figure, but we have since expanded our analysis to include scenarios to consider the distribution rates and exit activities through various economic environments; we now forecast the full-year 2024 US VC fundraising to reach $58.8 billion in a downside scenario, $79.3 billion in a base-case scenario, and $92.1 billion in an upside scenario.

Although economic uncertainty has subsided since 2023, LPs are still contending with a prolonged high-interest-rate environment and persisting skepticism regarding startup valuations. As a result, they are scrutinizing opportunities more closely due to limited distributions. Despite the LP pullback, established managers such as Norwest Venture Partners and TCV both raised $3.0 billion megafunds, while Andreessen Horowitz announced raising $7.2 billion across multiple VC funds. General Catalyst is also reported to be raising $6.0 billion—approximately 20% of the current YTD 2024 fundraising value. While it is unlikely for fundraising levels to recover to 2021 and 2022 levels, investor appetite will most likely drive fundraising to meet the base-case scenario of $79.0 billion, well above the original $67.0 billion we used as a benchmark in 2023.

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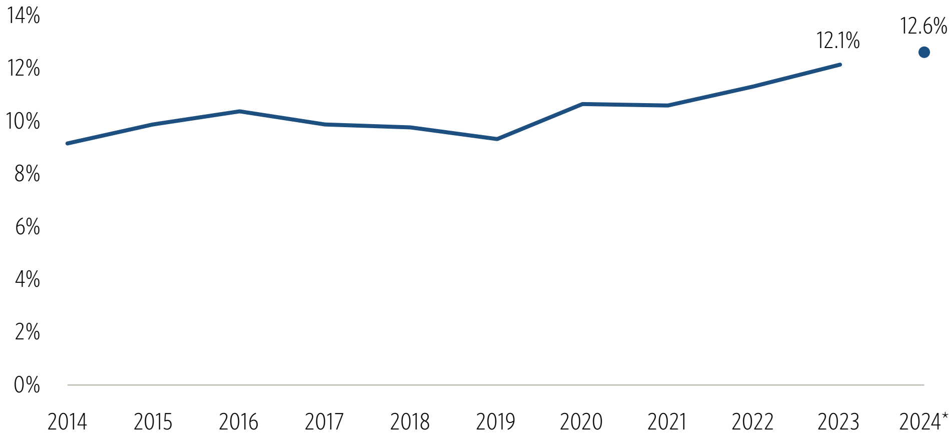
Outlook: The number of insider-led rounds as a proportion of all US VC deals will be on par with or exceed the 2023 annual level.

Insider-led rounds as a share of all VC deals



Source: PitchBook • Geography: US • *As of May 23, 2024

Rationale from December 2023

The percentage of US VC insider-led deals will stay elevated in 2024—at least for the first half of the year—due to the likelihood of the ongoing capital constraints and lingering market volatility, challenged investor confidence, and because exit channels have not reopened yet. Since mid-2022, US GPs have slowed the pace of dealmaking, and many institutional LPs have faced liquidity issues, with the denominator effect being a contributing factor to those with public market exposure. With information asymmetry, existing investors have a more in-depth understanding of their portfolio company's performance and growth prospects. Insider-led rounds can help push out new pricings until a benchmark that matches market expectations has been hit, rather than drastically pushing down a company's valuation through pressure from new investors.

The number of insider-led rounds where at least one lead investor is from the existing syndicate as a proportion of all US venture deals ticked up from 11.5% in 2022 to 12.8% in 2023 YTD. Because a turnaround in the financing market is not expected in 2024, insider rounds will likely take up a larger portion of US VC deals across the venture lifecycle compared with the historical level. This pattern will be particularly pronounced at the late stage, where the imbalance of capital demand and supply has reached its highest level in nearly a decade. Mature companies collectively face an acute capital shortage challenge because of the pullback from crossover investors and the poor exit environment keeping such a high number of companies private. Good companies with sought-after products and solid unit economics are always able to raise capital—in good markets or bad—but startups that have been unable to gain traction or hit the next milestone will likely flounder in light of the financing difficulty.

Midyear update

The equity funding drought lingered through the first half of 2024. With a lack of clarity on when the Fed will start cutting interest rates and the magnitude of those cuts, as well as an overall sluggish exit environment, investors remained highly selective for making deals. While dry powder for the US VC ecosystem is currently sitting at a record high, a significant portion of those uncalled LP commitments are held by megafunds, most of which have remained cautious. Due to their fund size, many of these megafunds focus on late- and growth-stage startups—the valuation of which has yet to rebound from recent compressions—and are still subject to macroeconomic headwinds.

In a challenging fundraising environment, existing investors are stepping up to help portfolio companies that struggle to secure external equity financing. While there has been increased interest in exploring nondilutive financing options by investors and companies, lenders have also become highly cautious, opting to lend only to the highest-quality companies that have at least 12 to 18 months of runway while also showing strong revenues and stable cash flows. The lending criteria translates to companies that are running low on cash being unlikely to find success in obtaining venture debt.

For startups that hold the potential to grow and scale but have not achieved cash flow break-even, existing investors may try to cobble together a round that is just large enough to tide them through the financing winter. The hope is that companies will get to the next inflection point at a time when the market sentiment improves, and that they will be in a better position to gain traction from new investors.

During the first half of 2024, the number of insider-led rounds where at least one lead investor was from the existing syndicate as a proportion of all US VC deals continued to tick up and notched 12.6%, as compared with 12.1% in 2023. The phenomenon is particularly pronounced at the late stages of the venture lifecycle, as mature startups that typically need significant cash infusion have been facing severe headwinds from a capital supply shortage issue. As of H1 2024, the number of rounds where at least one lead was a follow-on investor as a proportion of all VC deals climbed to 14.1% and 20.1% for the late and venture-growth stages, respectively. The percentage of deals led by insiders has reached the highest level across early, late, and venture-growth stages and is expected to stay elevated unless we see meaningful improvements in capital supply.

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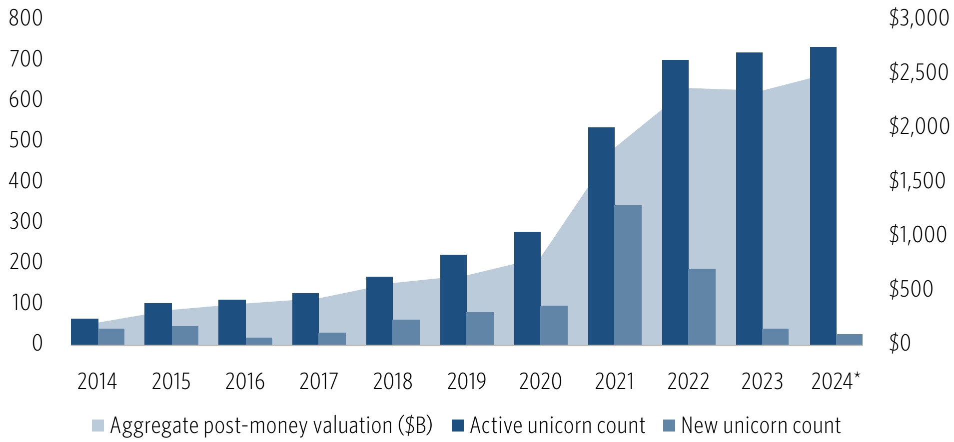
Outlook: US active unicorn count and aggregate post-money valuation will decline in 2024.

Unicorn count and aggregate post-money valuation



Source: PitchBook • Geography: US • *As of May 23, 2024

Rationale from December 2023

This year's slower growth of new unicorns, with 43 insofar, is a far cry from the 188 seen the year prior and on pace to hit a six-year low. The unmistakable discrepancy between public and private valuations has made investors more cautious of inflating valuations without supportive financial metrics. While the number of active unicorns has continued to grow, the aggregate post-money valuation has plateaued at a high of $2.4 trillion.

As some of the largest unicorns anticipate going public, taking down rounds prior to listing could be a way to level set investor expectations and assure share value growth. As more unicorns deplete cash runways and struggle to turn profitable, we should anticipate more returning to raise in the harsher dealmaking environment, which could potentially force them to compromise their valuation to stay alive.

The decline in active US unicorns and their aggregate post-money valuation would have knock-on effects on the US VC market. The current record-high unicorn aggregate value is indicative of the inflated valuations and remaining value trapped in funds. As aggregate value falls, the residual value stuck in this subset of startups will also decrease and pave the way for more accurate return modeling based on adjusted valuations; unicorns that go out of business will free up remaining investor dry powder to support other startups; and IPOs will help generate liquidity, prompting the recycling of capital back into the venture ecosystem.

Midyear update

Despite strong headwinds, aggregate unicorn post-money valuation and count continued to climb in the first half of 2024. The higher-interest-rate environment has continued to dampen exit activity, staving off potential IPOs, while only five unicorns have raised a down round. This coupled with the robust deployment of capital into AI has led to unicorn valuations and counts sidestepping the obstacles laid out before the start of the year.

In Q1 2024, the number of flat and down rounds as a proportion of all VC deals reached a decade high of 27.4%. High interest rates, and the hangover from lofty valuations, remain prevalent risks to current unicorns. The surprising resilience of aggregate unicorn value can partially be attributed to the concentration in the largest names like SpaceX and OpenAI. Decacorns are responsible for 37% of the value while making up only 5% of the population. Therefore, to see a drop in aggregate value, it would likely have to correspond with down rounds from these decacorns, like we saw from Stripe last year. For now, the opposite has been occurring. There have been no decacorn down rounds, likely due to these companies' ability to access forms of capital other than new equity. However, there have been seven up rounds that added $113.5 billion in aggregate value. If this trend continues, it is hard to imagine a scenario where enough down rounds from smaller companies can negate the increases from the decacorns.

This year, 14 unicorns representing $23.9 billion in value have exited, failed, or lost unicorn status because of a down round. These counts have been offset with 29 new unicorns minted in 2024, on pace to beat the dismal numbers from last year but below any previous period between 2018 to 2022. The most notable of these is xAI, which raised at a valuation of $24.0 billion, completely negating the value lost due to exits, failures, and down rounds. AI continues to be a dominant investment theme in the market. Although it has been over a year and a half since the launch of ChatGPT, investor appetite for AI exposure remains consistent. The enduring appetite for AI exposure has served as a surprising catalyst for unicorn creation, with AI companies representing nearly 45% of new unicorns and over 60% of the added value.

Shifting to the back half of 2024, the market expects interest rates to remain high, pricing in only two cuts before the year's end. With this environment in place, the market should mirror the timid activity seen thus far. Given the prevalence of capital allocation toward AI and the lackluster exit activity, it is unlikely we will see unicorn value or count drop without seeing startling weakness in the largest names.

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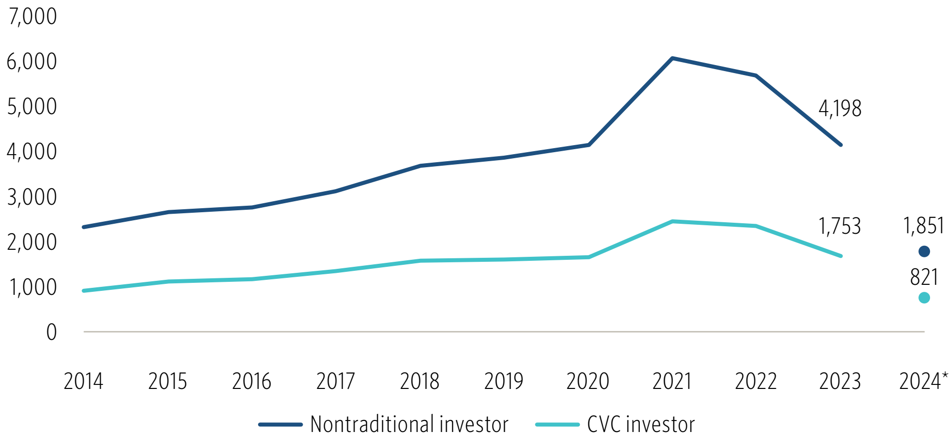
Outlook: Flat or declining interest rates in 2024 will lead to an increase in US VC deal activity with nontraditional VC investor participation.

Count of investors that made at least one deal by investor type



Source: PitchBook • Geography: US • *As of May 23, 2024

Rationale from December 2023

Since Q2 2022, we have seen a sizable exodus of nontraditional investors from the venture ecosystem, coinciding with the Fed's rate hikes that began in March 2022. While these declines are palpable, there are some encouraging signs that could bring more nontraditional investors back into the venture ecosystem in 2024. Stable or declining interest rates alter the risk-return profile of assets, as investors search for better returns as the opportunity cost of forgoing traditional fixed-income investments decreases.

Declining interest rates may also have a positive impact on public equity valuations as the present value of future cash flows increases in a lower-interest-rate environment. This could lead to increased company valuations in public markets, which for nontraditional investors that have portfolios comprised of both public and private securities, such as crossover investors, could free up allocation space for VC.

The risk-return profile is also of particular interest for corporate venture capital (CVC) investors; private startups have been plagued by declining valuations and a lack of capital supply from traditional investors, thus creating a unique opportunity for corporate investors looking for both a financial and strategic return. While many CVCs have remained engaged in the venture market in pursuit of discounted investment opportunities, many more are likely to join or rejoin the space should the prospect of VC investing become relatively less risky in a lower-interest-rate environment.

Midyear update

Heading into 2024, the market was expecting up to eight rate cuts from the Fed, but as it currently stands, rates remain unchanged. With the fed funds rate sitting at levels not seen since prior to the global financial crisis, investors face a significant opportunity cost allocating capital to longer-duration asset classes like venture. As such, many nontraditional investors have chosen to remain withdrawn from the venture market through the first half of the year, seeking shorter-duration asset classes where they can capitalize on higher rates with lower risk and more access to liquidity.

In 2024, unique nontraditional investor counts are on pace for their lowest level since 2019, and the current performance of venture remains uninspiring. Down rounds represented 17% of VC deals in Q1 2024, the highest since 2014, and the late-stage relative rate of value creation dropped to its lowest level in the same period. Add in the timid exit environment, and you have a risk-return profile that is unjustifiable by many nontraditional investors.

CVC investors face a similar allocation decision; however, suppressed valuations open the door for strategic investment opportunities. AI continues to be a battleground for strategic initiatives, representing just over 25% of the deals with CVC investor participation. As companies continue to develop a strategy around AI use cases, this may be an area where CVCs take the risk and deploy capital into the venture ecosystem.

It is unlikely we will see an uptick in nontraditional participation through the rest of the year. The market now expects just two rate cuts by the end of 2024, a far cry from the six to eight previously anticipated. Thus, it is more pertinent to focus on what would bring these investors back. The three main drivers would be lower rates, faster value creation, and a pickup in exit activity. A lower-interest-rate environment would diminish the opportunity cost of, and lower the hurdle rate for, allocating capital into venture. Secondly, a higher pace of value creation would make the venture return profile more attractive. Lastly, an increase in exit activity would lower the duration risk and return uncertainty associated with the asset class. If we see any of these changes occur, nontraditional investor activity should increase, but until then, many will remain on the sidelines.

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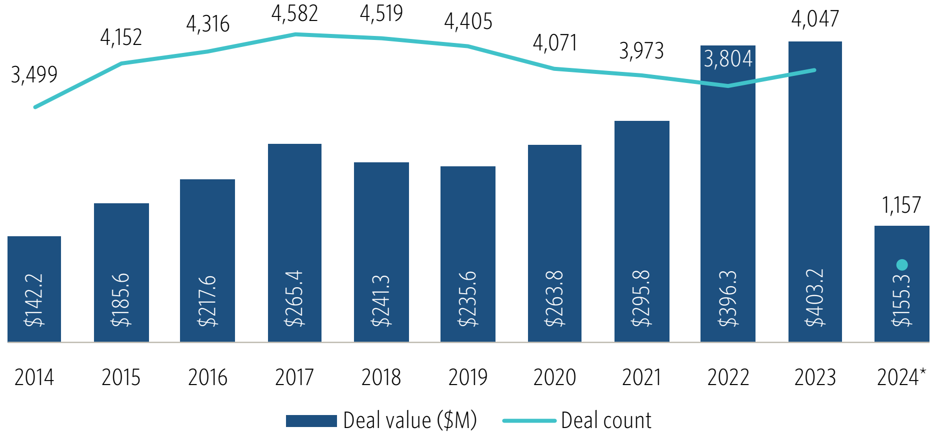
Outlook: Accelerators will play an increasingly important role with increased dealmaking momentum in 2024.

VC deal activity with accelerator and incubator investor participation



Source: PitchBook • Geography: US • *As of May 23, 2024

Rationale from December 2023

Amid a harsh financing climate, starting and running a company has become more difficult than any other time in the past decade, especially for first-time founders. In light of mounting headwinds, programs and entities that nurture the earliest stage of startup formation, most prominently accelerators and inception-stage-focused investors, are set to play an increasingly important role. Those programs or entities are heavily education-oriented, aiming to help founders ideate, build out their first minimum viable product, expand networks, and familiarize themselves with fundamental concepts such as go-to-market strategies.

As budding companies move to a future financing round, seed investors look for more developed business ideas and products and signs of traction. In this sense, the need for accelerators and investors that help founders ideate upon startup inception increases. The steady expansion of pre-seed alongside accelerators has made the earliest phase of venture more robust than ever.

From an accelerator perspective, they are active at the earliest phase of venture to bring in capital, expertise, and industry contacts to facilitate growth of nascent companies in exchange for equity at a low valuation. Accelerators are incentivized to take full advantage of the overall quality of founders to help bring their startup to the next level. As a result, we expect to see accelerators becoming more active in terms of deal volume in 2024.

Midyear update

There have been several developments in the accelerator ecosystem in 2024. Techstars closed multiple accelerator programs, winding down those in Seattle, Boulder, Austin, and several other nonhub market programs, and realigning its focus on San Francisco, New York, and other tech hubs. Google and NVIDIA launched a joint venture by combining their accelerator programs, while Microsoft and Alt Capital launched an early-stage AI-focused accelerator of their own. None of these necessarily showcase the increasing or decreasing importance of accelerators, but the negative reaction to Techstars' decision tells a story of reverence for how the accelerator programs impact local startup ecosystems, and the partnerships of Big Tech and AI have been the story of VC throughout the past couple years.

Data shows an interesting trend as well. 2023 had more capital invested in accelerator deals than any other year, and 2024 is well on pace for another strong showing of deal value through the first half of the year—accelerator and incubator financing data is some of the most lagged in VC. The number of active accelerators has remained incredibly high, as well. Already, nearly 1,500 investors have participated in accelerator rounds globally. The increase in accelerator programs over the past few years has surely impacted this statistic.

The more important data related to the importance of accelerators in this environment is the slowdown in seed-stage investment and the heightened deal sizes and valuations at that stage of the market. The statistics signal the high bar companies need to reach to secure funding at the stage, a much different market trend than a few years ago. In Q1, the median pre-seed and seed deal sizes reached nearly $1 million and $3.1 million, respectively, the highest level in the data. At the same time, investor stakes acquired during these rounds reached record highs as compensation for the risks being taken at the stage. With pre-seed and seed activity continuing to slow, startups are pressured even further to provide potential investors with more information and higher metrics, and to show lessened risk profile. Increasing or decreasing importance of accelerator programs may be somewhat subjective, but better development early on can have an enormous impact on success in this environment.

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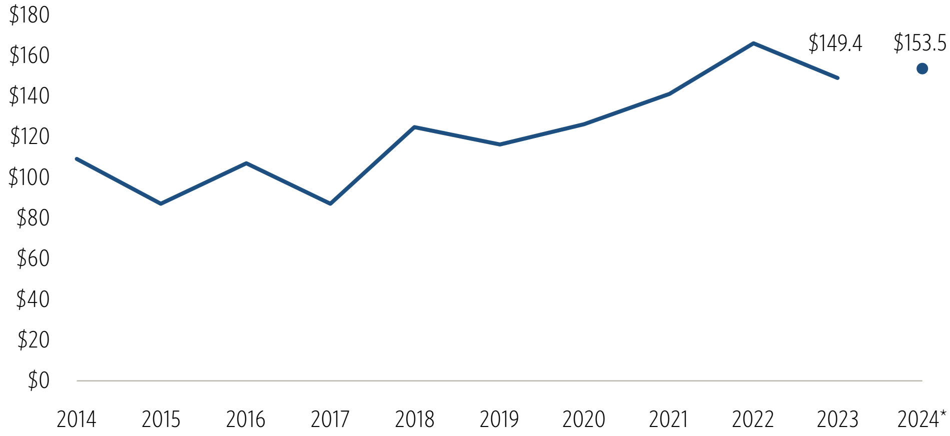
Outlook: The average US VC fund size will decline in 2024.

Average VC capital raised ($M)



Source: PitchBook • Geography: US • *As of May 23, 2024

Rationale from December 2023

In recent years, market tailwinds propelled US VC fundraising activity upward, setting consecutive annual record highs in terms of capital raised. Over the past few years, the average fund size grew more than 50% from $108.3 million in 2019 to $166.3 million in 2022. The favorable economic environment drove VC firms to raise larger funds at a much faster clip to seize the earmarked LP capital. Entering 2024, however, the era of billion-dollar funds has shown signs of slowing, with just 10 such funds closing through 2023 YTD.

Many of these funds frantically deployed capital in recent years into the most expensive venture market we have seen, and their interim fund performance is suffering from markdowns due to the slide in private valuations and the retreat of public company values. The lack of exits and distributions has discouraged LPs from committing to new venture funds, so they rebalance their portfolios instead into less risky assets with more stable returns. While there are and will continue to be firms that close billion-dollar funds, the changing dealmaking landscape and diminished LP appetite for venture has made repeating successful closes more difficult.

As a result of fewer large funds being closed, the average fund size declined 14.7% from its record high to $141.8 million through November 2023. We anticipate that the average fund size will decline further in this coming year as managers recalibrate their target fund sizes to appropriately capture LP interest and to participate in a market with adjusted valuations and deal sizes.

Midyear update

As mentioned in our Q1 2024 PitchBook-NVCA Venture Monitor, in Q1, the average fund size hit the lowest figure since 2017 ($104.6 million), and the median fell to the lowest figure since 2015 ($22.5 million). Not only did few large funds close—just four closed on more than $500 million—but few funds were closed of any size. The quarter put the year on pace for the lowest year of fundraising since 2017.

In the first couple weeks of Q2, Andreessen Horowitz announced the close of $7.2 billion across several new funds, Norwest Venture Partners closed a $3.0 billion fund, and Evolution Equity Partners closed $1.1 billion for its third technology fund. Even those few funds can have an outsized impact on the average seen across the market, especially when relatively few other funds are closed. The average fund size has blown past last year's figure, hitting $153.5 million, and that is without the inclusion of General Catalyst's $6.0 billion fund that is reportedly closing soon.

The true narrative of the fundraising market is not the average size of funds but the difficulties raising from LPs because of the poor exits and low distributions, which the above anecdotes highlight. At the time that data for this note was pulled, just 181 funds had been closed in 2024, pacing the year for the lowest annual total in a decade. The market is also positioning pricing power further into established manager hands. Andreessen Horowitz's funds' total was nearly 80% of the total raised in Q1. If General Catalyst closes its fund in Q2, established managers will have raised more in the first six months of this slow fundraising year than emerging managers have in total over the past 18 months.