PitchBook

Index of Venture-Backed IPOs

Q3 2021 update

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Introduction

The IPO market has been red-hot for US venture-capital (VC)-backed businesses in 2021, smashing records for both deal value and count—$513.1 billion and 221, respectively—through the end of Q3. These public listings have also come with healthy step-ups for private valuations, illustrating the strong demand from institutional investors for growing businesses. Given this extremely active public listing environment, we wanted to revisit our PitchBook VC-backed IPO index to investigate the post-listing performance of recent IPOs to see if that success has held up in the aftermarket. The full methodology of the index can be found at the end of this note, and you can find our initial release of this data here.

It is uncertain whether this sharp uptick in newly public companies can be sustained, as the rapidity of new listings is tracking at an unprecedented rate—nearly keeping pace with some of the activity levels from the IPO flurry of 2000 to 2001. Currently, at least 1,291 companies valued at more than $500 million are under VC backing globally, 744 of which are based in the US. Because the near-record year of 2021 has logged only 221 public listings through Q3, this inventory of IPO candidates implies a distinct possibility that the pace of listings could continue—especially given the pace of unicorn creation and mega-deal financings, which have topped 600 in 2021. This mismatch of IPOs to mega-rounds speaks to the rising inventories of large private companies under VC backing that have built up in the market over the last 10 years.

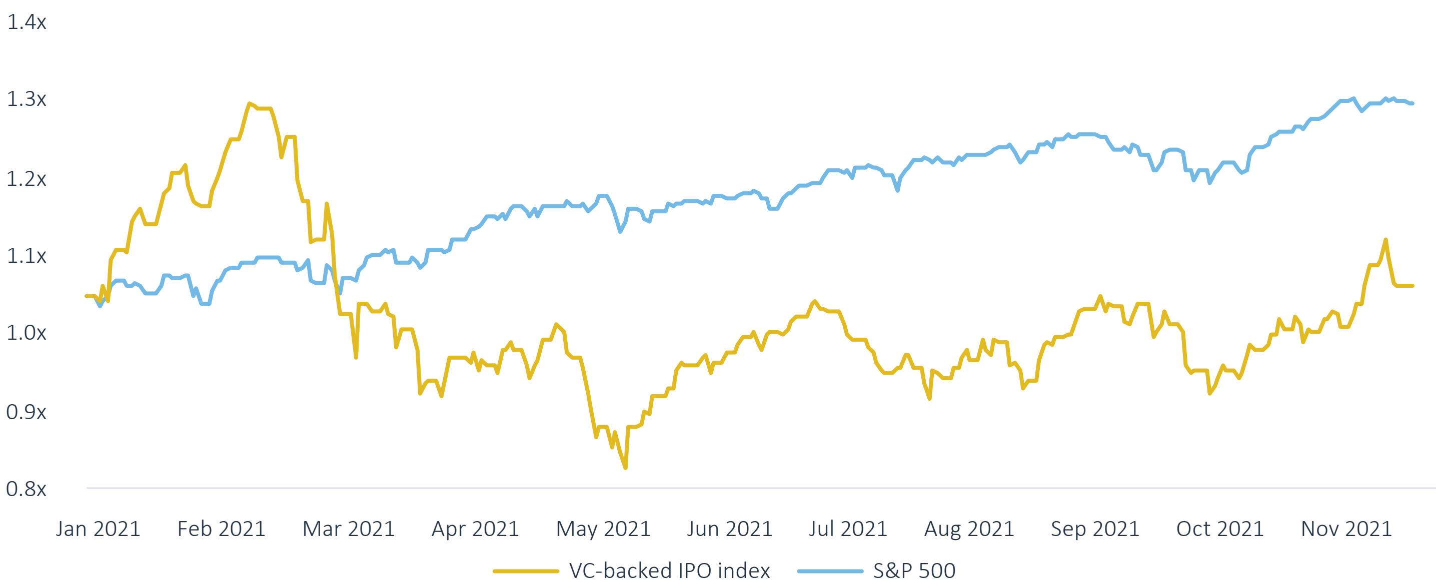
A massive inflow of VC capital in the last few years has driven this unicorn creation. The VC market has matured and attracted increasing amounts of capital from nontraditional investors, which has enabled companies to reach elevated valuations without facing the scrutiny of public markets. That logjam of companies big enough to go public and feasibly survive has finally started to batter its way through the floodgates and provide some liquidity for private backers and employees.

It is still a little unclear if the public listing activity in 2020 and 2021 was just a rush to the exits while the window remained open and market valuations were high—or if this rapid activity will continue for the foreseeable future. The threats of rising interest rates and macroeconomic shifts remain ongoing risks for the public markets, which are key to the strength of the IPO market.

Q3 2021 update

If we look at the performance of VC-backed IPOs at the beginning of 2021, we recorded some significant underperformance against the S&P 500. Most of the decline started around March, which roughly coincided with the initial period of rising bond yields and inflation concerns. Since then, VC-backed IPO performance has paced comparably flat relative to the market, sustaining the performance deficit.

YTD VC-backed IPO index against S&P 500

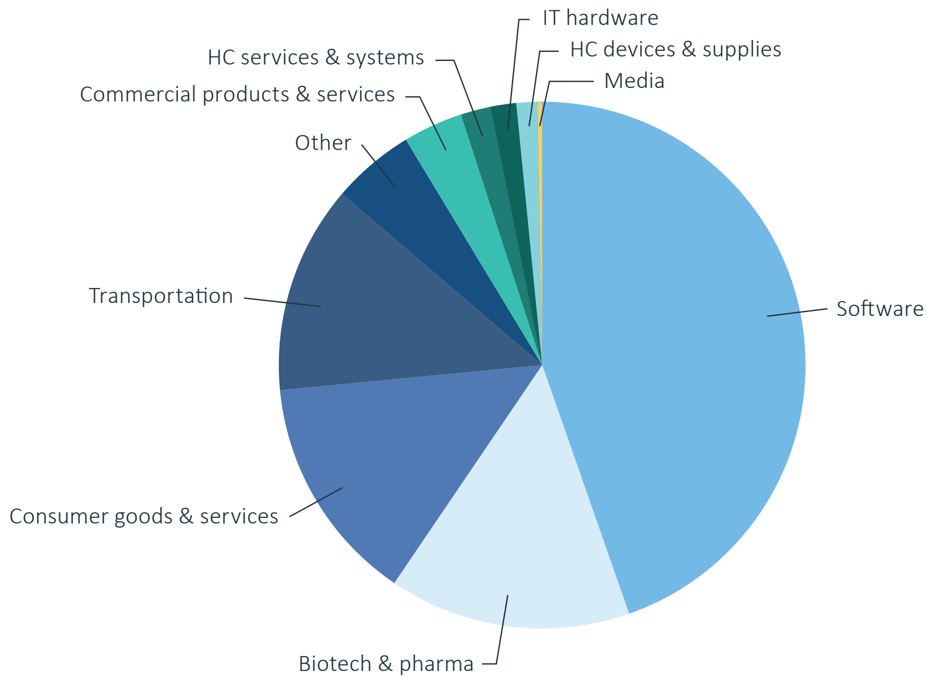


Source: PitchBook | **Geography:** Global
*As of November 23, 2021

There has been significant hype around IPOs of venture-backed businesses during the last few years. According to Jay R. Ritter at the University of Florida, the average first-day pop in 2020 was 41.6%, which is the highest data point since 1999 and 2000.[1] First-day pops are not included in the index—so we are missing out on a relatively large portion of return for IPO investors or private backers that remained on board through IPO. There have been some intriguing developments around investing in public shares of previously VC-backed businesses. For example, Sequoia Capital restructured its Sequoia fund to allow it to hold portfolio companies for indefinite periods after an IPO. This is a single example but also a serious data point that challenges the argument that most company value creation happens in the private markets. The lines between the public and private markets continue to blur as companies grow larger under VC backing, harkening back to the accelerating number of VC financings over $100 million. While Sequoia's move may not encourage copycats to adopt the permanent capital model, clearly, companies succeeded in creating value after transitioning to public markets. The handful of home-run investments VC investors may make over the long term are key to driving above-average returns for a firm. It makes sense to continue supporting the growth of these exceptional businesses as a financing partner, even as the company moves past traditional VC backing.

1: "Initial Public Offerings: Underpricing," University of Florida, Jay R. Ritter, December 29, 2020.

VC-backed IPO index industry breakdown*



Source: PitchBook | **Geography:** Global
*As of November 23, 2021

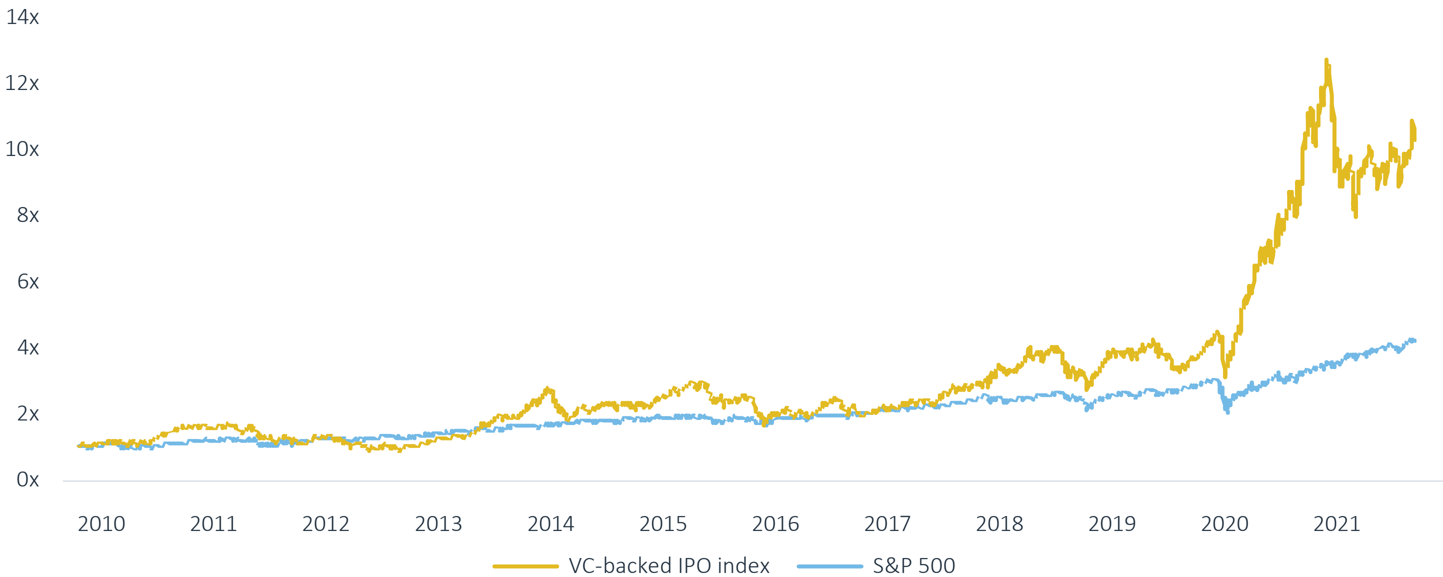
This attention from investors has also allowed valuation step-ups at exit to swell to near-term highs at a median 1.67x for public listings through Q3 2021, the highest we have tracked since 2009. This comes against a background of unabated growth of late-stage VC valuations, implying that comparable valuations have grown even more rapidly in the public markets. Public market valuation multiples—especially those of technology and, more specifically, software companies—are at all-time highs. The S&P 500 price-to-sales ratio is at 3.15x as compared to 1.77x in December 2000, and it only crossed 3.0x in April 2021, even though the current uptrend started with the March 2020 market weakness triggered by COVID-19.[2]

2: "S&P 500 Price to Sales Ratio by Year," Nasdaq, November 6, 2021.

Long-term performance

When we zoom out to the entire period we have tracked, VC-backed IPOs have performed incredibly well against the broader market, especially in the last few years. Our index shows that the greatest outperformance for VC-backed IPOs started around the time the market began recovering after the onset of the pandemic, when we recorded huge amounts of market cap value accruing to companies that had recently listed. We attribute much of this to the innovative VC-backed software and biotech businesses, which fared comparably well during the pandemic.

VC-backed IPO index performance since inception



Source: PitchBook | **Geography:** Global
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Companies such as Zoom Video Communications (NASDAQ: ZM), Moderna Therapeutics (NASDAQ: MRNA), CrowdStrike (NASDAQ: CRWD), Pinterest (NYSE: PINS), Peloton (NASDAQ: PTON), and others drove this massive run-up in 2021 performance by adding tens of billions of dollars in market cap. Many of these businesses were positioned to directly capitalize on some economic shifts that came about due to the pandemic, but being tech heavy relative to the S&P 500 has also been a boon, as these companies benefited from the above-average rise in technology valuation multiples.

Outside of the spike in 2020, the outperformance of the S&P 500 by VC-backed IPOs since 2014 has been relatively consistent, which is an encouraging sign for the VC ecosystem and the harmony of valuations between the public and private markets. Clearly, a significant amount of value creation is happening in the private markets; however, there is still growth to be found after the IPO.

Methodology

To introduce the product, we are diving deep into the rationale behind the methodology to help fully explain what the different indices are displaying.

Population

- Every VC-backed IPO included is listed on the New York Stock Exchange and Nasdaq, regardless of company headquarter location. We chose this broader geographical scope to better reflect the investments of the developed VC participants, who may have diversified strategies investing across Europe, China, and the US.

- Companies must debut with a post-money valuation of more than $50 million to be considered for inclusion.

Reconstitution

- Newly listed companies that fit the criteria are first included beginning the first day of the quarter after they exit via IPO, and continue to be included until the first day of the quarter after they have been trading for two years. For instance, a company that completed an IPO in February 2018 would have been included during the March 31, 2018, rebalance and dropped out at the March 2020 rebalance.

- In addition to normal deletions from aging out of the two-year window criteria, companies will also be removed from the index following an acquisition or bankruptcy or if their market cap falls below $50 million at any rebalance. If the event falls in the middle of the quarter, these companies are removed at the next rebalance date.

- Companies can be added to the index on a more expedited basis: If a company falls in the 95th percentile market cap of companies in the index, it will be added the day after its IPO.

- All index weights are rebalanced quarterly or in the event of an inter-period addition or deletion.