PitchBook

European Venture Report

Q1 2020

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Introduction

VC deal activity started the new decade admirably with the fourth-strongest quarter ever in terms of deal value. We anticipate dealmaking to slow considerably as the repercussions of COVID-19 sweep across the globe and highly valued, mature startups taper growth efforts. However, follow-on rounds will remain popular and late-stage investments in existing portfolio companies will take priority.

Deal value involving CVC participation slowed in Q1 2020 after the record-setting 2019. CVC arms will tighten up investment strategies as recessionary fears surface and impacts across different sectors vary considerably.

Healthcare VC investment may decrease to a lesser extent than other sectors. Funding could become critical in the current fight as well as in the aftermath of the pandemic. Opportunities within telemedicine, drug discovery and logistics have been identified due to COVID-19.

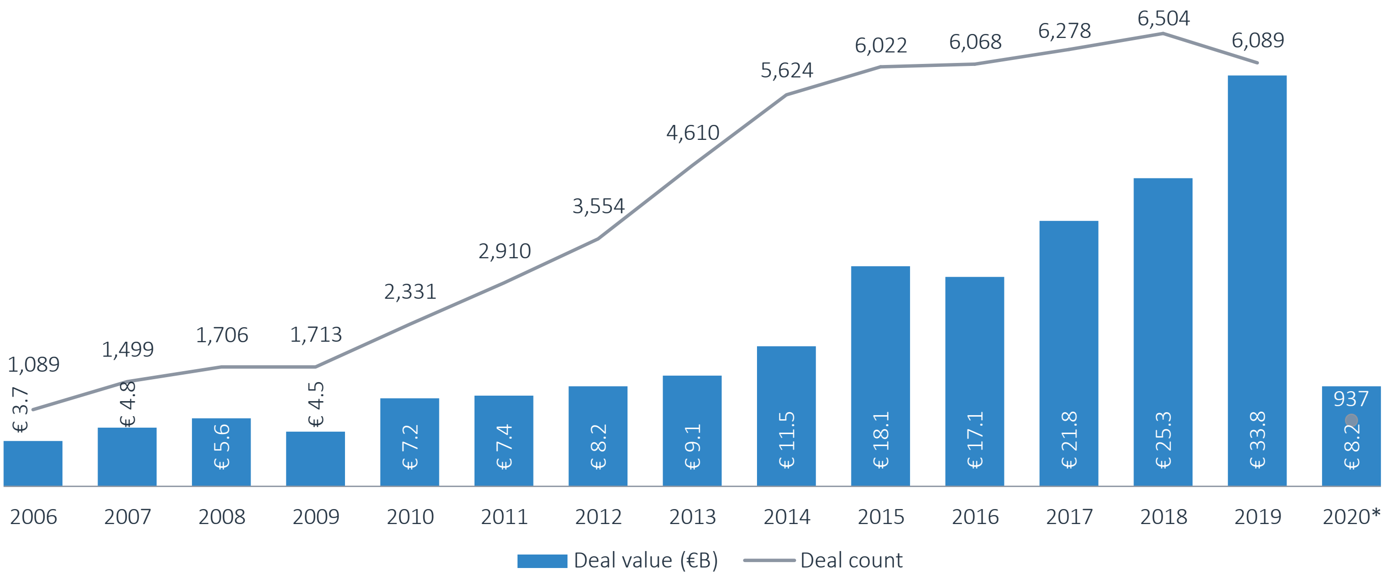
The VC-backed exit market started 2020 cautiously, and this is likely to continue. Despite uncertainty, the two largest exits in Q1 2020 originated from the promising Ireland ecosystem. Listings and acquisitions are likely to remain muted as volatility in public markets and valuation risk increase.

Fundraising commenced 2020 in very strong fashion. Despite this, we believe fundraising levels will dip during the rest of 2020 as closed funds fall in frequency due to lockdowns. Newly closed funds have continued to grow, and deployment strategies may need to be recalibrated due to COVID-19. LPs may re-evaluate commitments given the impending economic downturn.

Nalin Patel
Analyst, EMEA Private Capital

Overview

VC deal activity

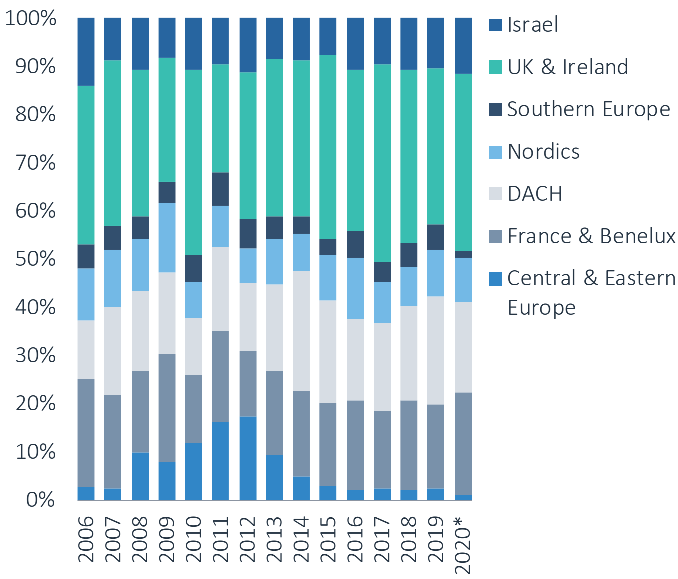


Source: PitchBook | **Geography:** Europe
*As of March 31, 2020

Following a record year of deal activity, European venture kicked off the new decade with the fourth-strongest quarter ever in terms of total deal value, reaching €8.2 billion. We expect dealmaking to slow considerably in the next two quarters, however, as the repercussions of COVID-19 sweep across the globe. We believe the bull run sustained over the last decade may finally be coming to an end as wider economic outlooks considerably weaken. Dealmaking will not collapse, but this is the toughest economic challenge facing the venture ecosystem since the global financial crisis (GFC).

For the first two months of the quarter, it was business as usual. However, the rapid spread of COVID-19 within Italy in early March confirmed that a pandemic was unavoidable in Europe. The continent's largest economies, including the UK, France, Spain and Germany, joined Italy on lockdown within a matter of weeks. The unprecedented but necessary measures have had severe implications on startups, VC investors and LPs, all of whom rely on the intertwined, globalised and democratic European markets for goods and services. Sizable deals completed in Q1 2020 or filtering through currently were likely negotiated prior to the widespread disruption in Europe or pushed through in anticipation of future issues.

VC deals (€) by region



Source: PitchBook | **Geography:** Europe
*As of March 31, 2020

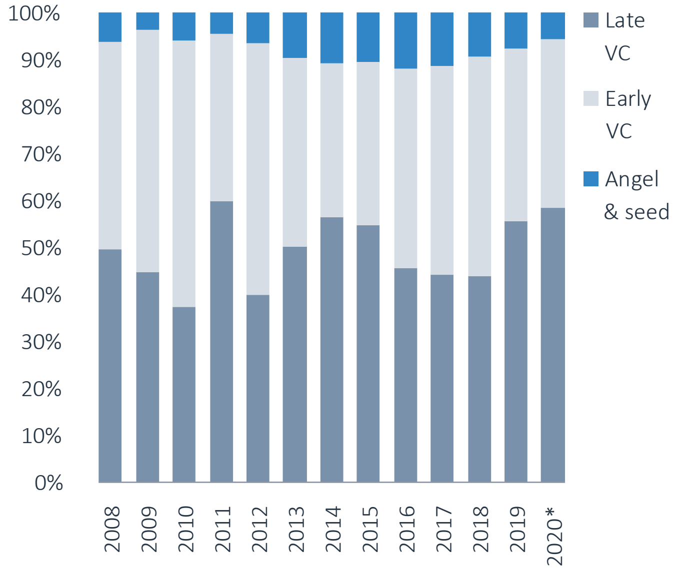
Overview

Revolut secured €451.0 million in the largest deal to close in Q1 2020, using the timely round to launch its bank app and card in the US. It follows heavyweight European fintech companies N26 and Monzo in their recent expansion across the Atlantic. Revolut compete for US market share not only against international fintech players but domestic startups such as Chime and Varo as well. Fintech has emerged as one of the hottest subsectors in which to work and invest during the last decade. Demand for online banking may increase in the short term amid lockdowns, but we believe mature fintech companies will taper aggressive growth strategies in 2020 due to COVID-19. Fintech is the most crowded subsector in Europe, and its capital-intensive nature is compounded with relatively slim margins on financial products that need to be competitive. Many of these highly valued startups have accrued financial losses over fiscal years as they've focused on market share and scale instead of profitability. Nonetheless, we will see companies flatten or trim headcount in certain areas for the first time to shore up unit economics and protect business robustness.

Mature startups have used large swathes of late-stage capital to extend runways in 2020. VC firms pumped €4.8 billion into European late-stage companies in Q1, the third-highest quarterly figure on record. One such deal involved Klarna, which completed a €180.0 million round from follow-on investor Commonwealth Bank of Australia (ASX: CBA). Klarna's valuation now stands just shy of €5 billion, having raised €1.1 billion while in the VC ecosystem. The company has raised rounds regularly since 2010 and showcases how startups' unrelenting demand for capital has been matched by enthusiasm from international VC investors. Klarna has been able to re-engage existing and attract new investors with relative ease during the funding push over the last decade. Nevertheless, capital availability challenges could surface rapidly in the current climate, and leveraging investor networks could become vital. VC investors will not want to see their flagship startups fail, so we expect late-stage investments in existing portfolio companies to take priority over early-stage investments in the next year to ensure funding gaps do not appear.

The propensity to use capital in a follow-on rather than a first-time round has filtered through the ecosystem during the last decade. In 2019, 92.4% of venture euros went to follow-on deals. Capital in first-time deals has remained flat in the last five years, while follow-on rounds have doubled in total value. The shift could be compounded as countries undergo lockdowns in Europe. 78.9% of all deals have been follow-on rounds so far this year and we

VC deals (€) by stage



Source: PitchBook | **Geography:** Europe
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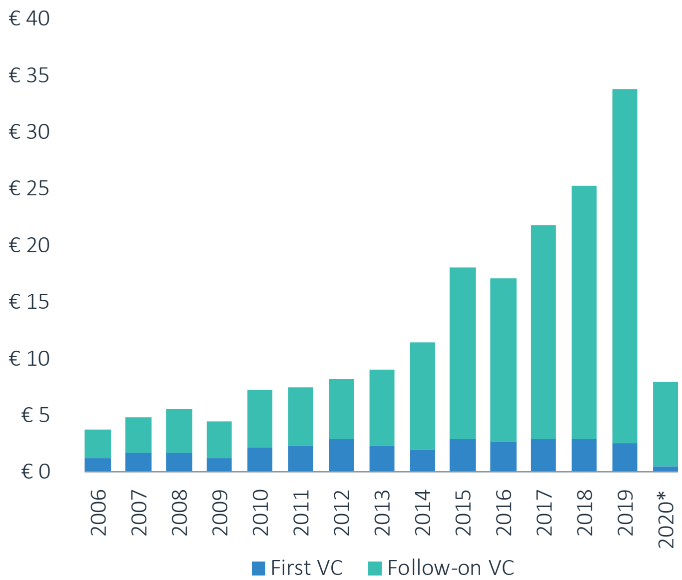
First-time and follow-on VC deals (€B)



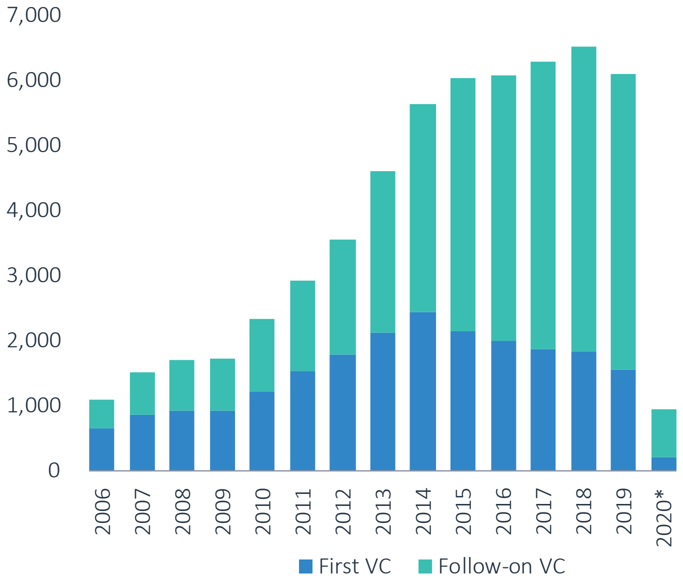
Source: PitchBook | **Geography:** Europe
*As of March 31, 2020

anticipate this figure will increase during 2020. The ability for GPs to develop new relationships with startups without meeting founders or employees will be significantly hindered. Therefore, we believe securing first-time deals will take longer and become more difficult in today's environment. VC investors will need to re-evaluate reserves for existing portfolio companies too, and this will have knock-on effects as the capital available for first-time rounds reduces.

No sector appears completely immune from the pandemic. Nevertheless, deals are still occurring across a variety of industries. While commercial passenger flights have been cancelled in the short term, both Lilium and Volocopter closed €217.1 million and €50.0 million rounds respectively in Q1 2020, to assist with their long-term visions for eVTOL aircraft. Widespread adoption of such technology is years away, but current economic conditions did not deter investors. In fact, Lilium's round was reportedly pushed through by China-based Tencent Holdings (HKG: 00700) to avoid future disruption to European economies, after Asian markets slowed to a standstill earlier in 2020. We believe there could be a lesser impact on long-term, research-based deals for non-revenue generating startups. Highly capitalised VC investors may look to complete deals in the next few quarters amid the looming downturn. They could benefit from more favourable negotiating terms, incorporating fewer founder-friendly clauses as startups with long-term visions burn through cash during the R&D pre-revenue stages of their lifecycle.

Software startups have accounted for 42.6% of capital YTD, and we believe investment will remain strong relative to other sectors in the coming months. Startups in the home-based working, online education and recreational activities spaces have already faced heightened demand. Germany-based Personio, which provides an online HR management tool, completed a €67.3 million round prior to lockdowns occurring. This deal exemplifies how startups that can assist remote collaboration and centralise essential functions online could see upticks in demand as businesses adapt to workforces not operating under the same roof. Opportunities will also be created for software startups focusing on personal cybersecurity, as scams and phishing attempts have reportedly increased on individual networks. Moreover, many companies will now look to improve preparedness and resilience of technical infrastructure as well as disaster risk planning procedures to ensure they are better equipped for future black swan events.

First-time and follow-on VC deals (#)



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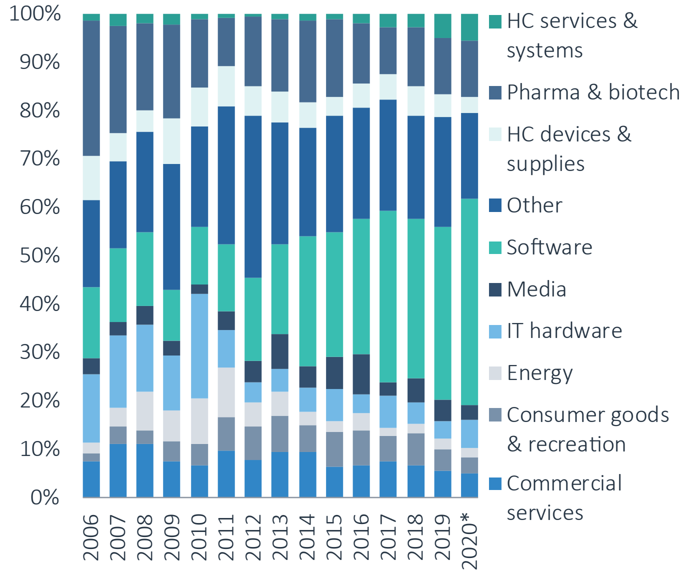
VC deals (€) by sector



Source: PitchBook | **Geography:** Europe
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PitchBook

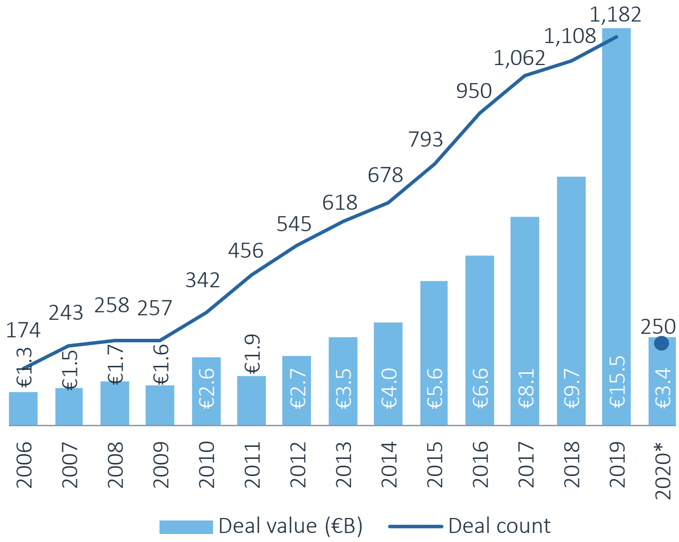
Corporate VC

Deal value involving CVC participation reached €3.4 billion during Q1 2020. The figure was lower than the quarterly average across 2019 and looks set to fall further heading into the rest of 2020. Deals with CVC investment have been increasing rapidly in terms of count and value over the last decade. We believe CVCs have sourced innovative VC investments to stay ahead of competitors and seek favourable returns. As we enter the new decade and confront a global recession, the pressure on corporates will intensify. Volatile share prices, trimmed earnings and a lack of demand have already had an impact on growth targets and forced corporates to slash or remove dividend payments to save capital. Global economic downturns are felt faster in more liquid public equities, and as focus quickly shifts to protection of core assets and revenue streams, CVC investment is likely to fall consequently.

The immediate and lasting consequences of COVID-19 will vary by sector. The automotive sector has been one of the hardest hit, and factory closures through April are forecasted to trigger a loss of €66 billion, equivalent to 2.6 million cars sales in Europe. At the start of the year, London-based electric vehicle unicorn Arrival secured a €100.0 million round from Hyundai (KRX: 005380) and Kia (KRX: 000270). Various traditional incumbents have been putting resources into electric vehicle development in recent years. It remains a long-term and capital-intensive strategy, but necessary as fossil fuel use diminishes and car manufacturers evolve to meet consumer demand. Electric vehicle adoption is limited in Europe in comparison to traditional combustion engines, but popularity is growing. European vehicle emission targets and regulations are among the most stringent in the world, particularly due to recent scandals and environmental lobbying. As the current crisis has seen car sales plummet, near-term financial health of major players will take precedent over long-term outward investments. Nonetheless, electric vehicle development will persist as previously set targets will need to be met in the coming years regardless of economic conditions.

We expect CVC arms will tighten investment strategies in the bear market and align them more closely to their parent core businesses. Opportunities will still arise with most of Europe locked down, and some sectors have seen upticks in service usage, especially in the home entertainment sector. Berlin-based music streaming service SoundCloud closed a €67.9 million round from US-based radio broadcaster Sirius XM (NASDAQ: SIRI) in Q1 2020. Despite the deal closing prior to sweeping lockdowns, startups in the sector could thrive as millions of people are advised to stay home. We expect awareness and usage of such services to increase for at least the next quarter. As individuals stay at home, independent creative entrepreneurs could also increase the supply of content on platforms such as SoundCloud. With less consumer spending on tourism and socialising, home-based entrepreneurs and social media influencers could see rises in popularity too. The pandemic will no doubt shape future spending habits, and this could be an opportunity for CVCs to invest in services targeting online spending.

VC deal activity with CVC participation



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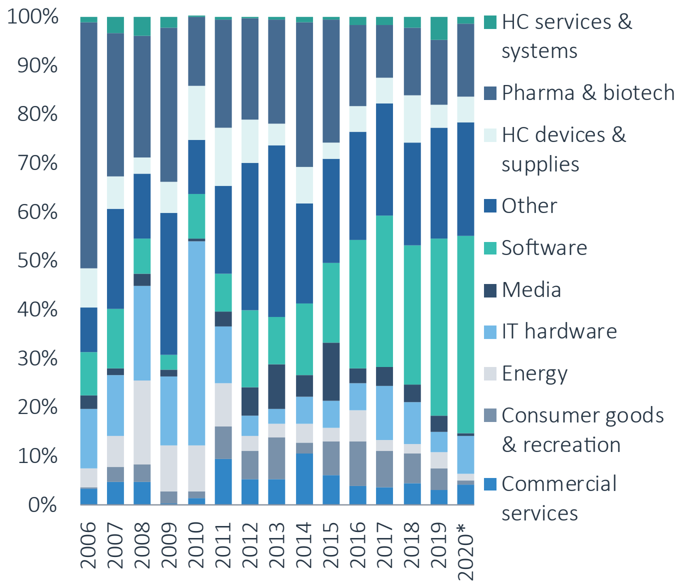
VC deals (€) with CVC participation by sector



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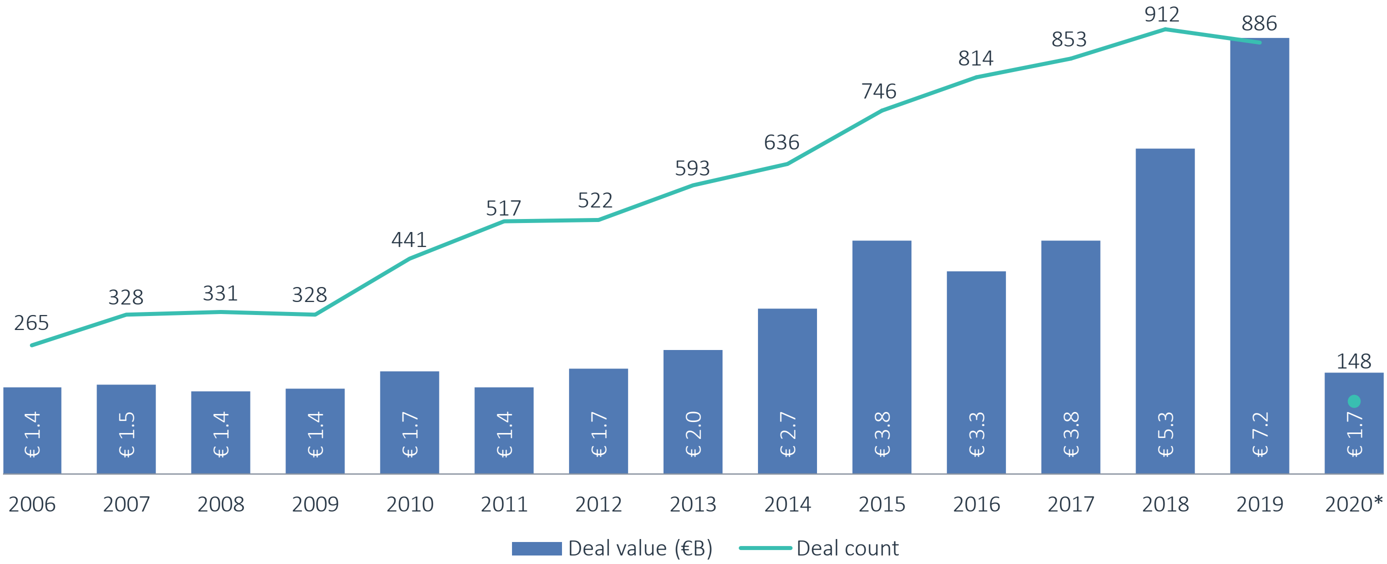
Spotlight: Healthcare

Healthcare VC deal activity



Source: PitchBook | **Geography:** Europe
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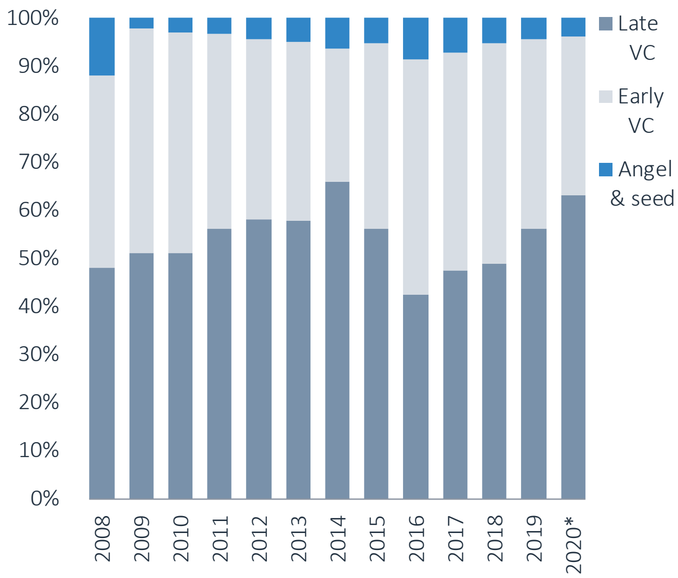
Healthcare startups attracted €1.7 billion from investors in Q1 2020. If the current pace is maintained during 2020, the annual total will near the record €7.2 billion achieved in 2019. However, we believe healthcare VC deal activity is expected to slow as recessions bite into economies. The impact on healthcare investment could be less noticeable than in other sectors, as funding will be critical in combating the devastating pandemic. Healthcare VC activity has ballooned during the last decade. Entrepreneurs have attempted to tackle issues facing the deployment of a large, highly skilled workforce in high-pressure environments delivering complex care services to a growing population, often with funding restraints. Startups focusing on technology-integrated solutions to assist with service provision, logistics, efficiency and drug research have made popular investment strategies.

A typically diverse collection of healthcare deals closed in Q1 2020. Deals such as London-based Immunocore's €154.3 million round and AM-Pharma's extension - which increased its round to €163.0 million - were able to close before COVID-19 gained significant traction in Europe. Both companies focus on long-term clinical stage trials for new drugs to treat diseases. We expect R&D and investment to reduce in the short term as healthcare resources are urgently channelled towards management of the pandemic. We do not expect capital-heavy long-term investments in drug discovery to stop, but attention and medical resources are currently fixated on COVID-19, and we expect this to be the case for at

Healthcare VC deals (€) by type



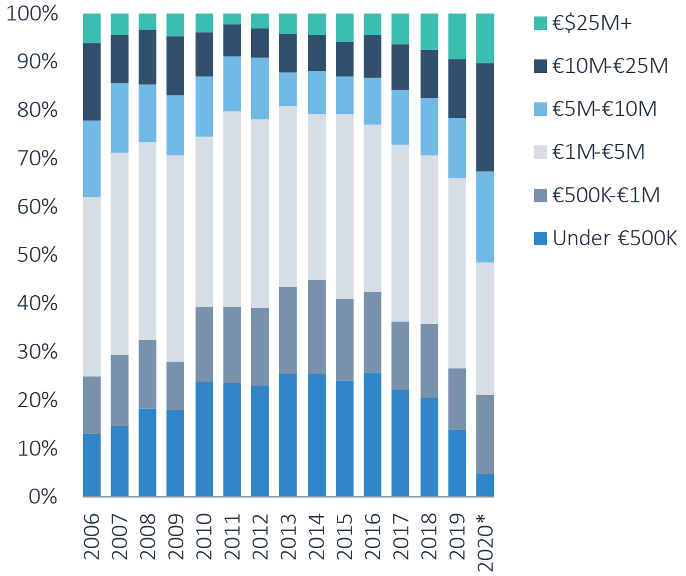
Source: PitchBook | **Geography:** Europe
*As of March 31, 2020

least the next quarter. This will create opportunities for healthcare startups that can shift focus towards drug research for the novel coronavirus.

Healthcare services have been evolving rapidly, and this pandemic could accelerate the need for and subsequent growth in startups focusing on telemedicine services. Stockholm-based KRY completed a €140.0 million financing in Q1 2020, one of the largest healthcare rounds of the quarter. Early indications have shown that demand for digital doctor services have surged in the last few weeks in Europe due to the highly infectious nature of COVID-19 in medical institutions. If demand continues to rise, with hospitals and general practitioner surgeries remaining off-limits to other patients, these digital healthcare startups could demonstrate significant revenue growth quickly. In fear of missing out, startups and investors could fast-track rounds to gain substantial market share swiftly. Lengths of lockdowns are currently unknown, and once lifted, the public may demonstrate stickiness with virtual services as major benefits include ease of use, time saved travelling and ultimately no risk of spreading or catching diseases. We believe rounds could be focused around telemedicine as a subsector over the next year. UK-based Babylon Health, another online doctor, recently developed and released a digital care assistant to advise people on how to diagnose and manage suspected COVID-19 infections. This further demonstrates how healthcare startups can support current management and future resilience against pandemics.

The extent of the pandemic has highlighted problems facing leading healthcare systems that have had been caught unprepared to deal with such a devastating virus. Shortages in essential equipment such as ventilators as well as protection for frontline staff such as aprons, gloves and masks have been reported in Europe. Logistical and supply chain issues have also meant that staff, stockpiles and resources such as oxygen may not have been redirected into hotspots as efficiently as possible. Moreover, government policy has come under fire as the trade-off between public and economic health of nations has been scrutinised. All these factors will create mass frustration in the short term. But the problems will also highlight glaring opportunities for investors and entrepreneurs to innovate and help prevent such panic. Once this difficult initial period is negotiated, there will be a recovery process, and hopefully healthcare startups can play a huge part in building resilience going forward.

Healthcare VC deals (#) by size



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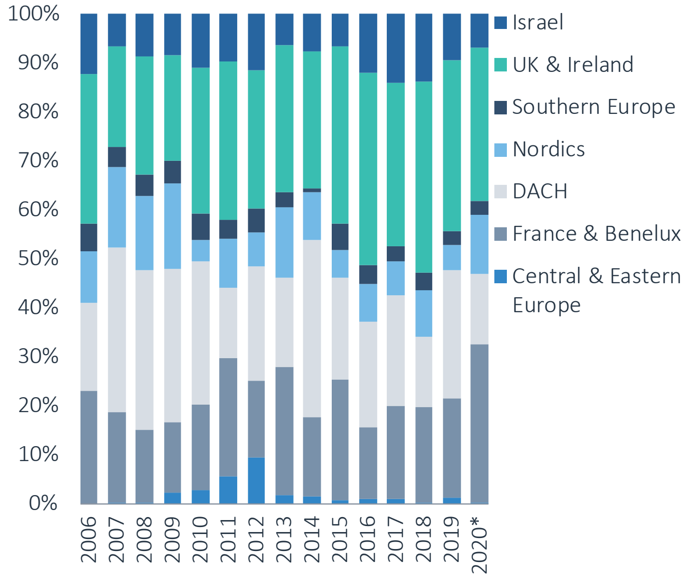
Healthcare VC deals (€) by region



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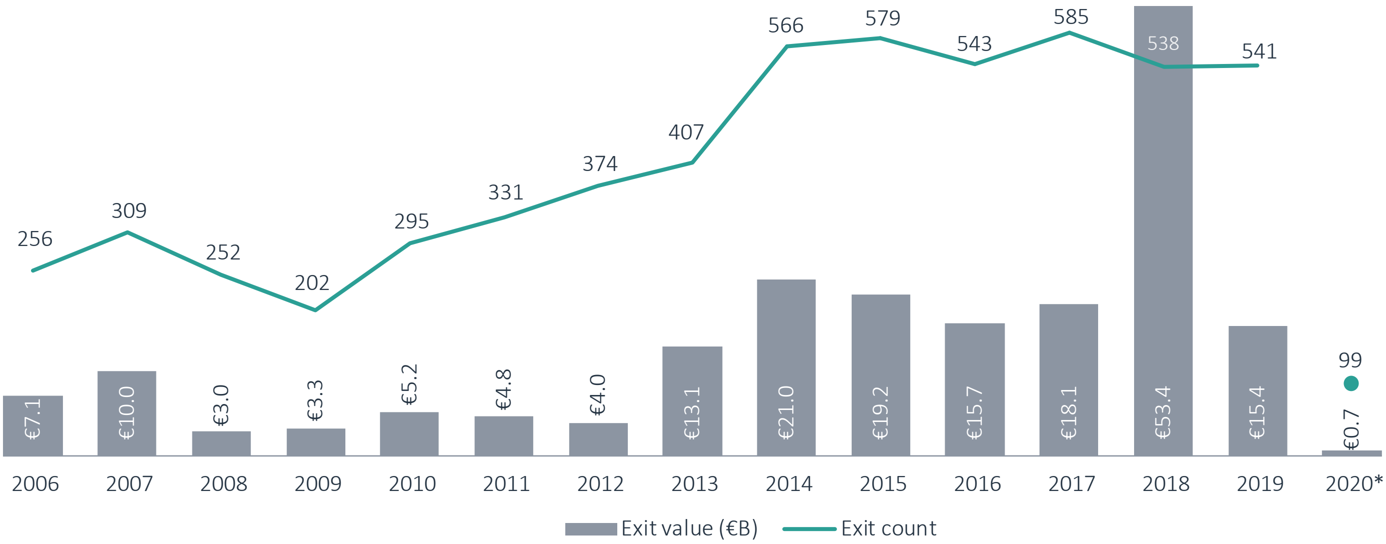
Exits

VC exit activity

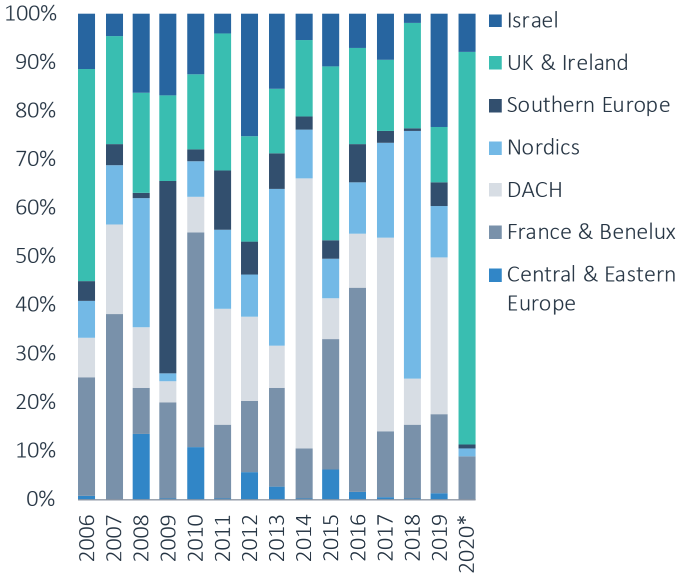


Source: PitchBook | **Geography:** Europe
*As of March 31, 2020

Exits totalled €727.1 million in Q1 2020, missing the €1 billion mark for the first quarter since Q4 2012. This represents a cautious exit market, which is likely to persist for the next few quarters. The impact of COVID-19 on exits is likely to be extensive, especially on IPOs and other types of liquidity that directly correlate to investor appetite and public equity performance. It is safe to say that the collection of highly valued unicorns in the ecosystem will be delaying exit plans for the foreseeable future, as economic impacts from COVID-19 are determined.

In Q1 2020, the two largest exits to occur in Europe were Ireland-based startups, indicative of the budding entrepreneurial environment developing in the country that has started to rival other well-established ecosystems. DecaWave's €369.5 million acquisition by US-based Qorvo (NASDAQ: QRVO) was the largest exit of the year so far. The Dublin-based startup specialises in ultra-wideband technology and provides solutions for mobile, automotive and IoT applications. The second-largest exit of the quarter belonged to Pointy, which was acquired for €146.4 million by Alphabet (NASDAQ: GOOGL). Pointy develops ecommerce inventory tracking tools for brick-and-mortar shops. Both strategic acquisitions underline how large US-based tech giants have continued to seek out emerging tech targets from European ecosystems. Acquisitions of Europe-based startups could attract a less expensive premium than US counterparts. They could also be far more appealing to startups looking to penetrate the lucrative US tech sector, rather than partner with a less experienced Europe-based corporate.

VC exits (€) by region



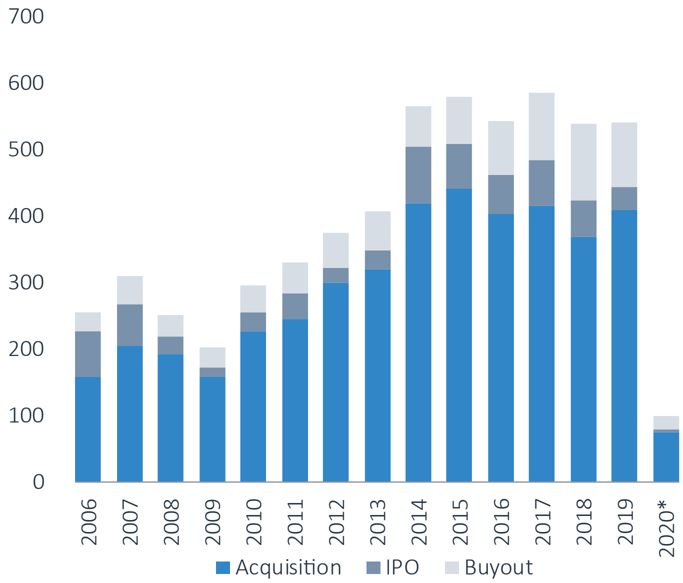
Source: PitchBook | **Geography:** Europe
*As of March 31, 2020

Only four VC-backed companies exited via IPO in Q1 2020. In 2019, the quantity of listings was precarious as speculation surrounding private valuations, an overheated market and an impending downturn cooled investor appetite. Nonetheless, no one could have predicted the aggressive emergence of COVID-19 shutting down European economies. The pandemic has all but ensured listings will be postponed for the foreseeable future, with many predicting that it could be six months before we see listings resume. The initial sell-off and subsequent volatility seen in public equities in recent weeks has been astonishing, as record swings have been reported with indexes and share prices. Before lockdowns across mainland Europe, telematics developer Munic listed at a €44.9 million pre-money valuation. Munic's share price dropped nearly 50% within three weeks of listing. It has recovered since, but this level of unpredictability will deter startups risking an IPO in the current environment.

Startups may not want to gamble on any kind of exit in present circumstances. However, there may be a lack of willing strategic acquirers in a position to complete exits too. Acquisitions accounted for 91.1% of exit value in Q1 2020 and have been responsible for the majority of exits every year on record. The drastic reduction in footfall will hurt revenues immediately for large corporates in transport and consumer-facing high street sectors. Corporates have closed temporarily across the globe, and focus will be placed on protecting core business lines rather than external growth. This will result in acquisition opportunities for startups reducing in the near term as corporates address the financial wellbeing of balance sheets first. The effect on corporates that rely on money and time spent online rather than in person will be affected to a lesser extent, as people work from home and deliveries continue. Corporates with strong cash positions could acquire startups—as they've done during previous black swan events—as asset pricings fall, and some will become distressed and may require immediate liquidity solutions.

Founders and investors will not want to see valuations of their best startups drop dramatically due to external market conditions. Investors may opt to close extension rounds to ensure the startup is attractive when the market rebounds, rather than see growth and value that has been nurtured over several years eroded within a few weeks. There are numerous unicorns in the ecosystem that we believe were ready for an exit in 2020. However, late-stage capital availability has altered how exits are perceived as a liquidity option in recent years. As COVID-19 has thrown financial markets into turmoil, we expect no unicorn exits for at least the next two quarters. Investors and management teams will instead pursue follow-on rounds to ensure these startups do not go out of business. Furthermore, as holding periods and exit horizon timelines are extended, we believe growth will slow and unicorns may flatten headcounts as recessions kick in.

VC exits (#) by type



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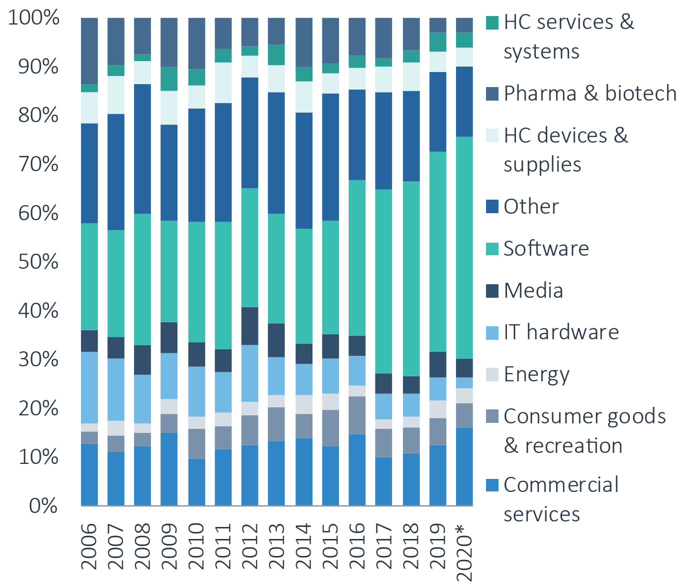
VC exits (#) by sector



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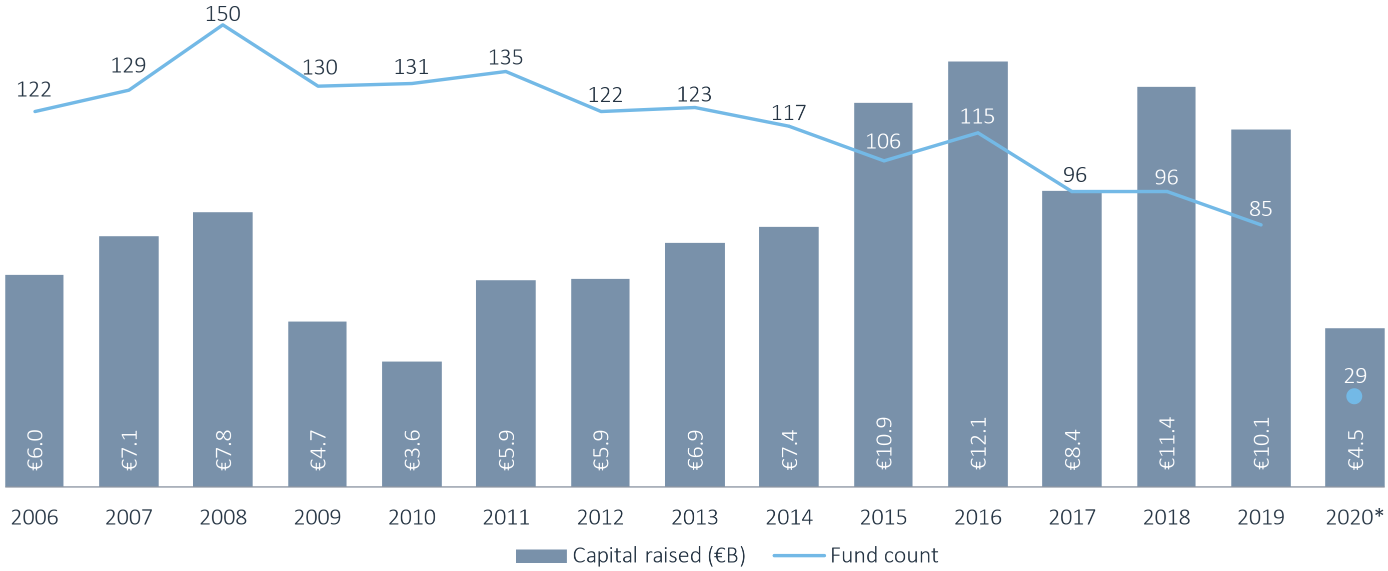
Fundraising

VC fundraising activity



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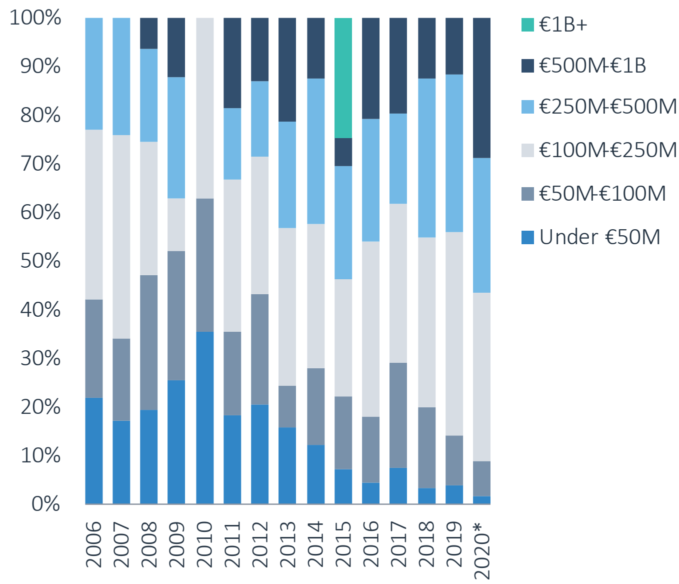
VC fundraising commenced the year strongly with €4.5 billion raised across 29 vehicles. During the last five years, European fund sizes have grown to compete internationally as commitments from LPs have increased. While funds closed in Q1 2020 present optimism, new and active fundraising efforts will be suspended in the short term as COVID-19 spreads across Europe. Funds that have closed in Q1 2020 are likely to have started and finished the capital raising process in the months before disruption descended upon Europe and the US. We expect fundraising levels to dip during the rest of 2020 as newly closed funds reduce in frequency.

Atomico's fifth venture fund closed at €746.3 million, making it the largest fund to close in Q1. It is the largest-ever London-based fund and one of the biggest venture funds to close in Europe. The recently raised vehicle puts Atomico in a considerably stronger position than its competitors, with the ability to deploy freshly raised capital where needed and take advantage of favourable terms that could arise for deals in a downturn. We believe the majority of newly closed funds will be directed towards existing GP portfolios in the near term to ensure financial wellbeing. The aforementioned fast-tracked Lilium round was in fact partially financed with capital deployed from Atomico, which underscores how pre-existing VC-backed portfolio companies could attract capital more effectively.

The diverging fortunes of portfolio companies due to COVID-19 will also create interesting dilemmas for GPs deciding where to deploy their freshly raised funds. Startups could be thriving and seeking capital to ride a wave of growth, while others could be struggling and require financing to help manage falls in revenue. For example, UK-based accuRx, a telemedicine startup, built a video chat tool within a week to help doctors and patients stay in contact, with 35,000 daily consultations reportedly taking place in the UK alone. AI supplier locating platform Scoutbee developed a new free tool to cope with a surge in demand from organisations in need of critical supplies helping to fight COVID-19. Both startups highlight how potential growth opportunities are forming in spite of and because of the virus. Furthermore,

VC funds (€) by size



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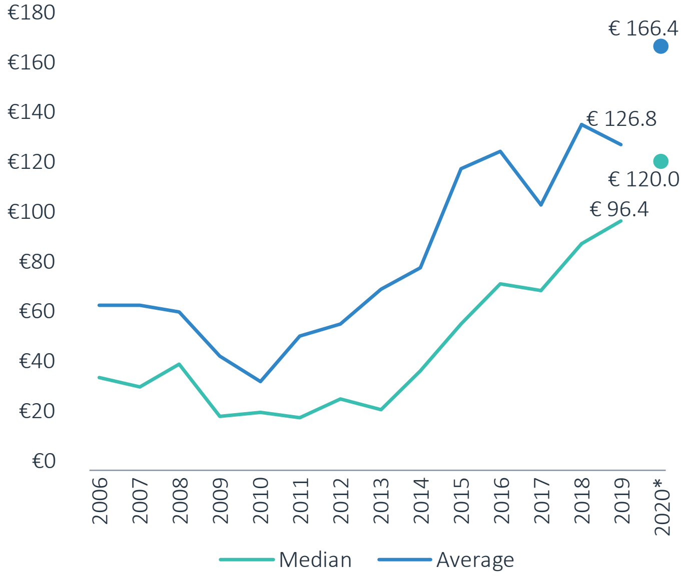
both companies have been backed by Atomico, which has also invested in startups such as Lime and Habito, which are facing different short-term fortunes. Lime has been forced to suspend scooter rentals in multiple cities, and online mortgage broker Habito operates in a sector that has seen demand significantly drop. This illustrates how delicate fund deployment decisions will be required to help existing portfolio companies weather the downturn, but also fund growth arising from short-term opportunities. The distribution of capital by GPs in the coming months could be critical to protect overall fund returns flowing back to LPs in the long term.

Amsterdam-based Life Sciences Partners (LSP) closed the largest-ever European venture fund devoted to healthcare technologies in Q1 2020. The €547.2 million LSP 6 fund surpassed its initial target of €396 million and attracted commitments from a diverse investor pool that included the EIF and healthcare giants Bristol-Myers Squibb (NYSE: BMY) and Otsuka Pharmaceutical (TKS: 4768). LP eagerness to commit to the fund personifies how fundraising has evolved for established GPs with a strong track record and extensive LP relationships. The recently closed vehicle could also play a huge part in supporting startups combatting the pandemic-induced crisis. As capital within the fund remains largely undeployed, it is now likely to fund COVID-19-related initiatives in the near term as medical attention and resources focus on the pandemic. GPs will also need to be prudent and not over invest in or become overfocused on these opportunities amid the panic, as healthcare systems and economies will rebound in the long term.

Funds in the DACH region have raised a strong €988.0 million so far in 2020, largely due to Zurich-based Lakestar. In total, Lakestar raised €678.0 million in Q1, with one-third going to Lakestar III for early-stage investments and two-thirds to Lakestar Growth I. Vienna-based Speedinvest also contributed a significant chunk of the total, closing its third-generation early-stage fund at €190.0 million. Speedinvest typically invests at the seed and early stages, and the oversubscribed and outsized nature of the fund portray how capital has been pouring into the ecosystem across all phases of the life cycle. It is reported that €100.0 million of the fund will be reserved for follow-on investments, and we believe this type of reserve strategy will proliferate in the ecosystem due to COVID-19. GPs that have raised capital recently will increasingly preserve it for their existing investments as travel restrictions and economic uncertainty make new rounds more challenging to complete.

VC fundraising is a high-risk and long-term investment strategy, and we could see LPs re-evaluate capital allocations in the recession. VC is not as volatile as public equities, nor does it enable the short-term liquidity flexibility for investors during a downturn. It is an illiquid asset class, and LPs may instead move capital intended for the ecosystem to fight fires facing other areas of their portfolio in the short term. Conversely, in the medium term, we may see LPs opt for long-term fund structures that could have a significant discount in comparison to pre-crisis levels. Unprecedented levels of capital have flowed into the European ecosystem from LPs across sectors and regions in recent years. Fundraising is a multi-year process, and we do not believe capital sources will radically fall in the long term, but LPs will be more cautious as an inevitable cash squeeze occurs.

Median and average VC fund size (€M)



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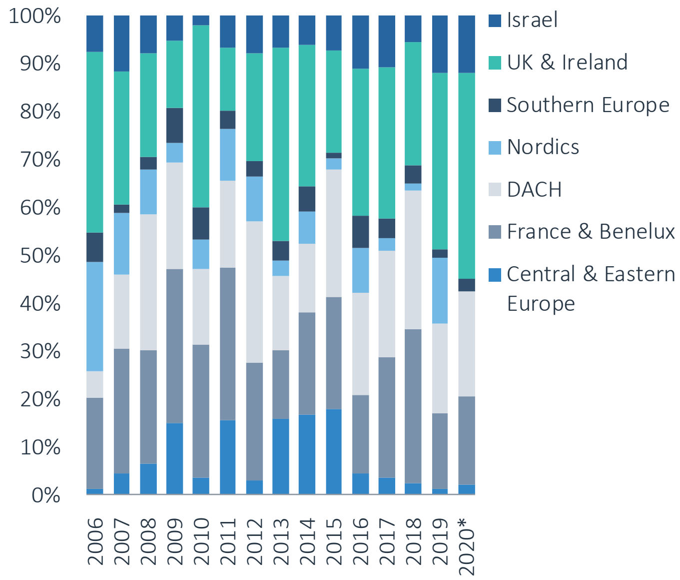
VC funds (€) by region



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