PitchBook

Q1 2023

US VC Valuations Report

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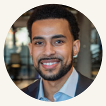

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Key takeaways

Adverse impacts resulting from a liquidity crunch and the market turning increasingly investor friendly have trickled down to the earliest stages of the venture ecosystem. The median seed pre-money valuation continued its growth trajectory since Q1 2020, reaching $12.9 million in Q1 2023. However, this expansion masks a survivorship bias, wherein revenue multiples have reportedly dropped significantly.

Declining economic conditions have continued to challenge the late-stage venture market, with the median deal size falling to its lowest level since Q2 2017. The demand for capital at the late stage is outstripping supply, with a capital-demand-to-supply ratio of 3.24x. This is due in part to the exit of nontraditional investors, which have been less active in the venture market, as well as a lackluster exit environment, resulting in a substantial decline in startup valuations. The median late-stage valuation in Q1 2023 decreased by 8.3% from Q4 2022, while the median late-stage VVC fell to $9.0 million, marking the first time it has dipped below $10.0 million since 2018. The challenging fundraising environment experienced thus far in 2023 is expected to persist, thus putting continued pressure on businesses at the top of the venture lifecycle.

Pressure is continuing to build in the venture growth stage, with the IPO window shuttered and investors' focus on profitability. As a result, the Q1 2023 median venture-growth pre-money valuation fell to $90.0 million, a dramatic decline from the 2021 full-year record figure of $355.0 million. Concurrently, the median deal size shrunk to just $7.0 million as investor appetite and risk tolerance for these types of deals waned. As cash runways are depleted, we expect an increasing number of these startups to resort to raising capital at flat or lower valuations in order to attract needed capital.

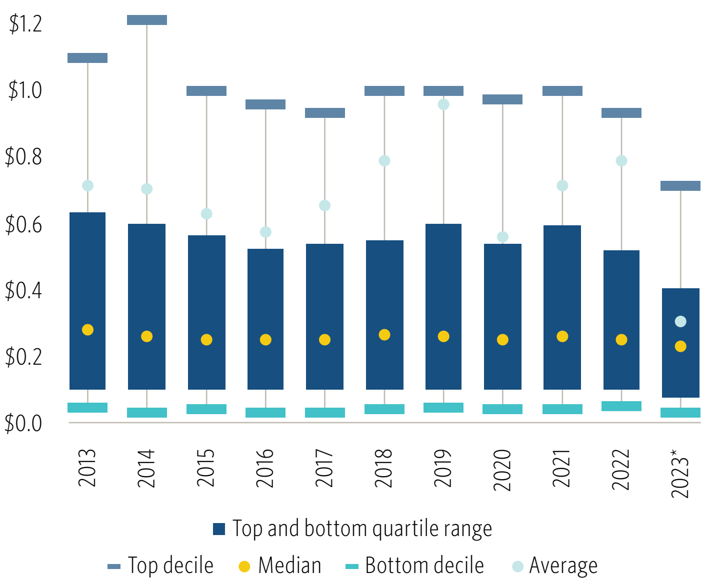
Nontraditional investors, crucial contributors of capital to late- and venture-growth-stage startups, have continued to pull back from the venture capital asset class due to a lack of liquidity. CVCs remain the exception to this narrative, notching a record participation rate on a deal count basis of 26.5% in Q1 2023. Their participation, along with other nontraditional investors, has allowed select startups to raise larger amounts of capital at valuations well above broader market medians, but it is not without cost as nontraditional investors have demanded larger equity positions for their continued involvement.

The dire state of public exits has continued through Q1 2023, during which only eight companies managed to exit via IPO. Despite a 42.3% quarterly increase in the median public listing VC exit valuation in Q1 2023, this figure is merely a fraction of that of the mid-2021 market exuberance. Healthcare startups made up half of public exits in Q1, and we expect to see a rebound in exit valuation when the public market warms to tech IPOs, which tend to generate outsized exit value.

Angel and seed

Median angel deal value lowest in decade

Angel deal value ($M) dispersion



Source: PitchBook • **Geography:** US
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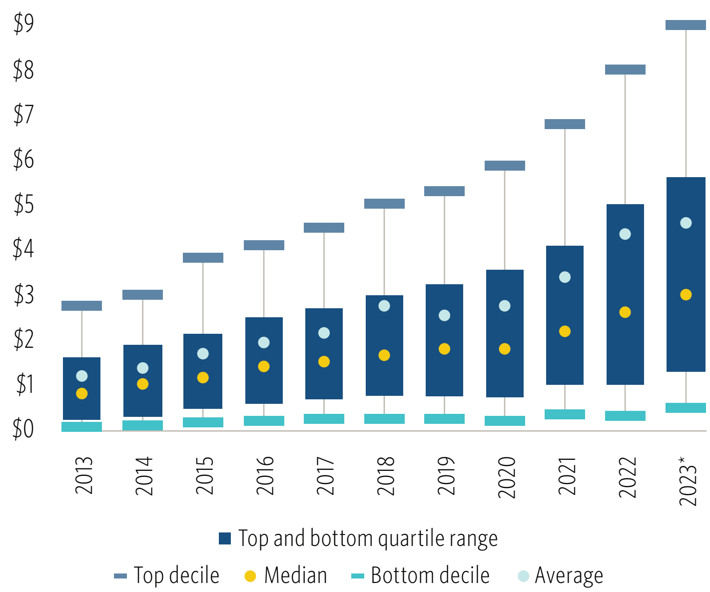
Seed deal sizes largest in dataset

Seed deal value ($M) dispersion



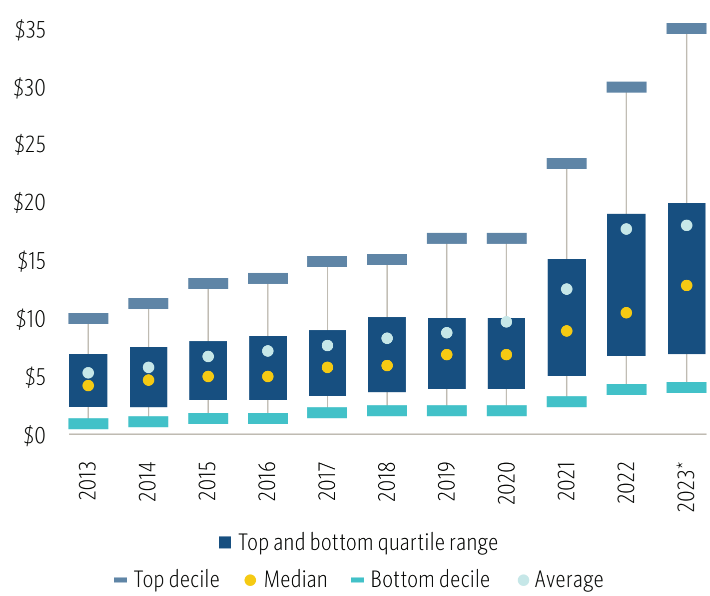
Source: PitchBook • **Geography:** US
*As of March 31, 2023

Sitting at the earliest phase of the venture ecosystem, angel- and seed-stage companies remained relatively insulated from the macroeconomic challenges inflicting their late-stage counterparts. However, adverse impacts from shrunken capital availability and the market becoming increasingly investor friendly have started to surface.

The median seed pre-money valuation has been on a consistent growth trend since Q1 2020. The figure rose by 16.9% over Q4 2022 to $12.9 million in Q1 2023 and stands 28.6% above the quarterly figure of one year ago. Two caveats lie behind the upward trajectory of median seed valuations. First, the selection bar for deals has gone up. To mitigate risks, GPs are writing checks only to companies with strong fundamentals, healthy burn rates, and solid strategies to preserve runway. This survivorship bias is corroborated by the median seed step-up expanding three quarters in a row and ticking up to 1.86x in Q1, attesting to how those carefully selected companies have been able to grow their valuations. The median time from founding for seed deals also witnessed a sizable increase, ascending from 2.4 years in 2022 to 3.0 years in 2023 so far, indicating that more established startups with relatively clearer growth trajectories as well as other metrics such as product-market fit can secure funding amid fierce competition.

Median seed pre-money valuation nearly reaches $13 million

Seed pre-money valuation ($M) dispersion



Source: PitchBook • **Geography:** US
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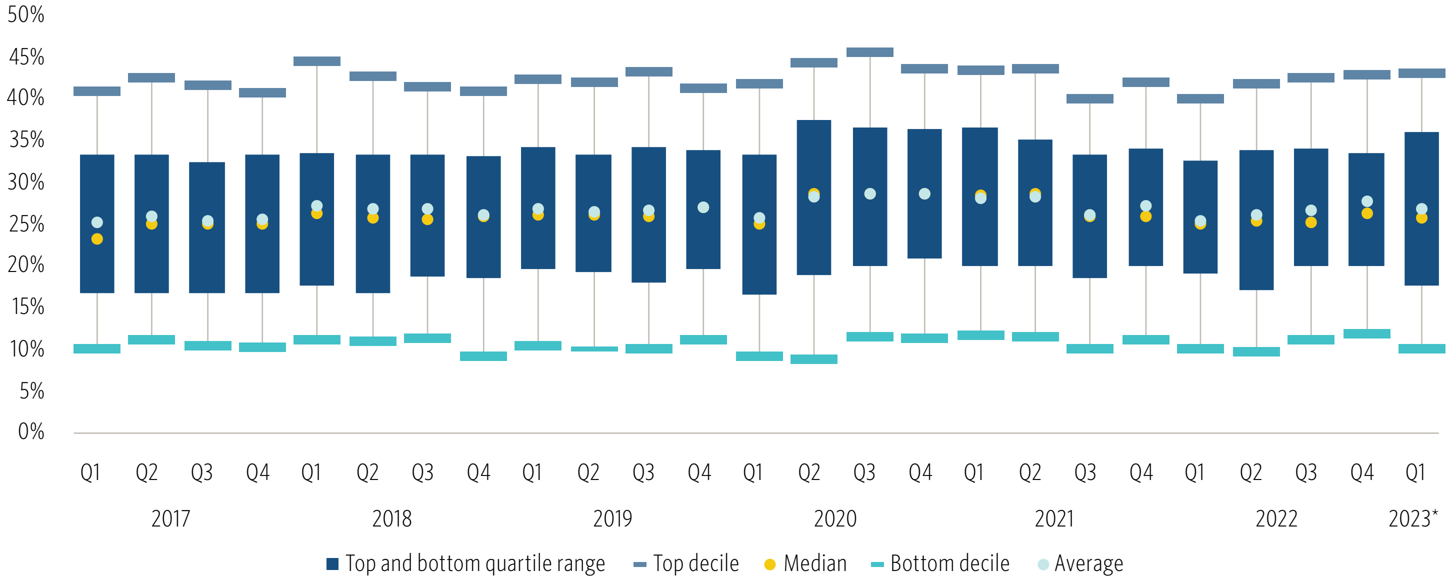
Seed share acquired highest since Q1 2018

Seed share acquired dispersion by quarter



Source: PitchBook • **Geography:** US
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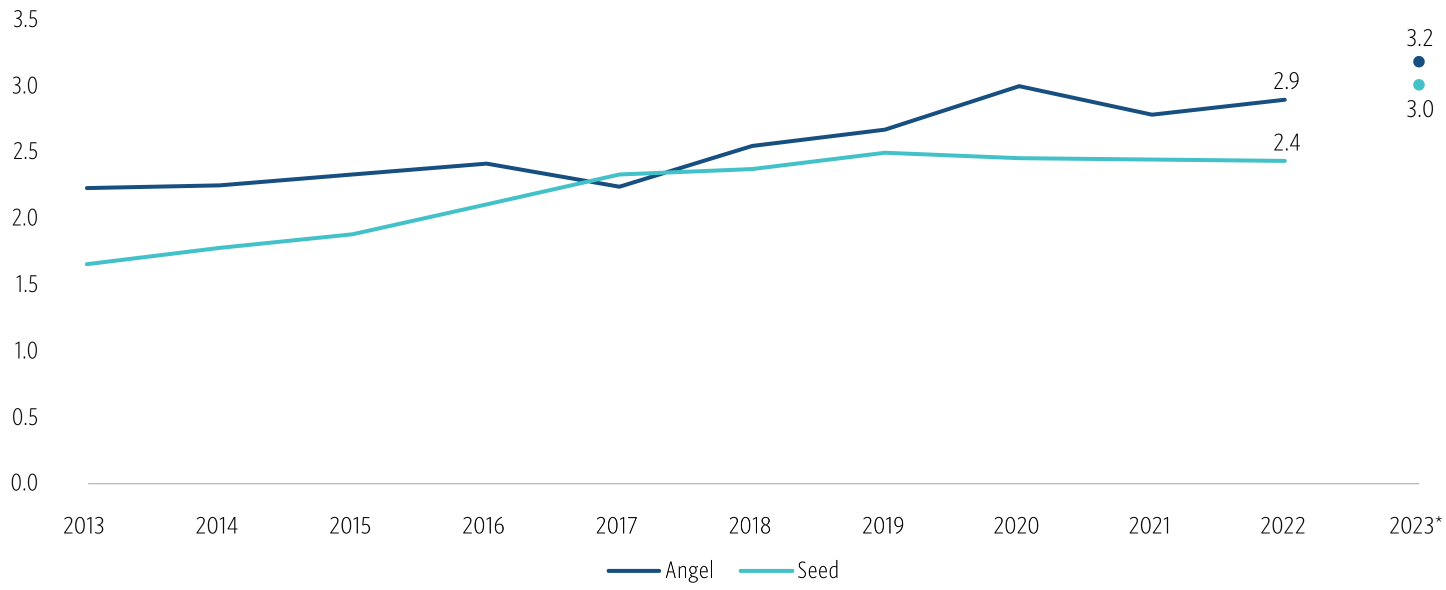
These increased benchmarks naturally reveal a survivorship bias in the data, wherein stronger companies are able to raise capital, while those that would have received smaller deals and valuations are excluded from the dataset.

The quarterly median share acquired for seed deals experienced a slight dip, landing at 25.7% in Q1. During the same period, the top and bottom quartile range reached the highest point since Q2 2020. This widened span points to a broad spectrum of seed deals, wherein investors could be asking for more favorable terms, negotiating more downside protection, and diversifying investments, as well as forming a syndicate to reduce risk.

Median age of company at seed round hits three years

Median time (years) from founding by stage

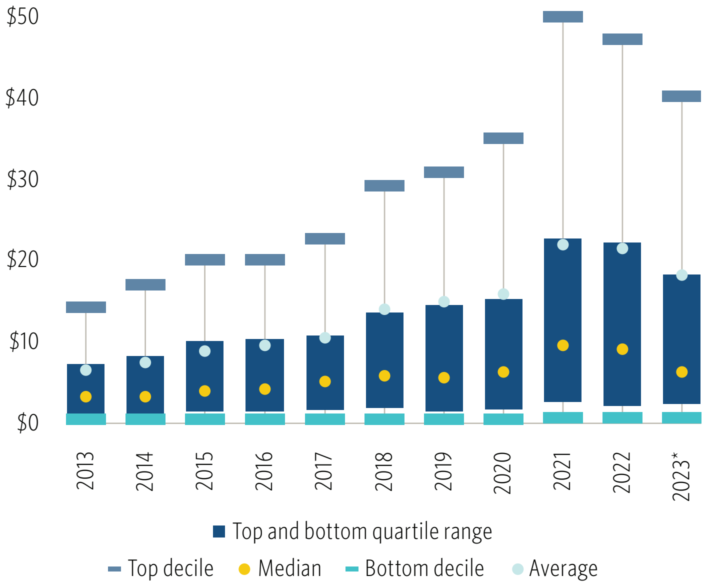


Source: PitchBook • **Geography:** US
*As of March 31, 2023

Early-stage VC valuations

Early-stage deal sizes continue to dip

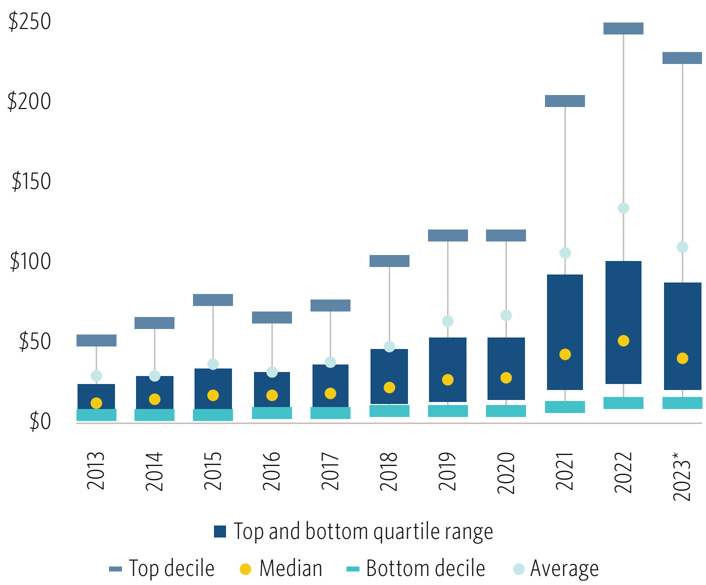
Early-stage VC deal value ($M) dispersion



Source: PitchBook • **Geography:** US
*As of March 31, 2023

Median early-stage VC valuation falls to eight-quarter low

Early-stage VC pre-money valuation ($M) dispersion



Source: PitchBook • **Geography:** US
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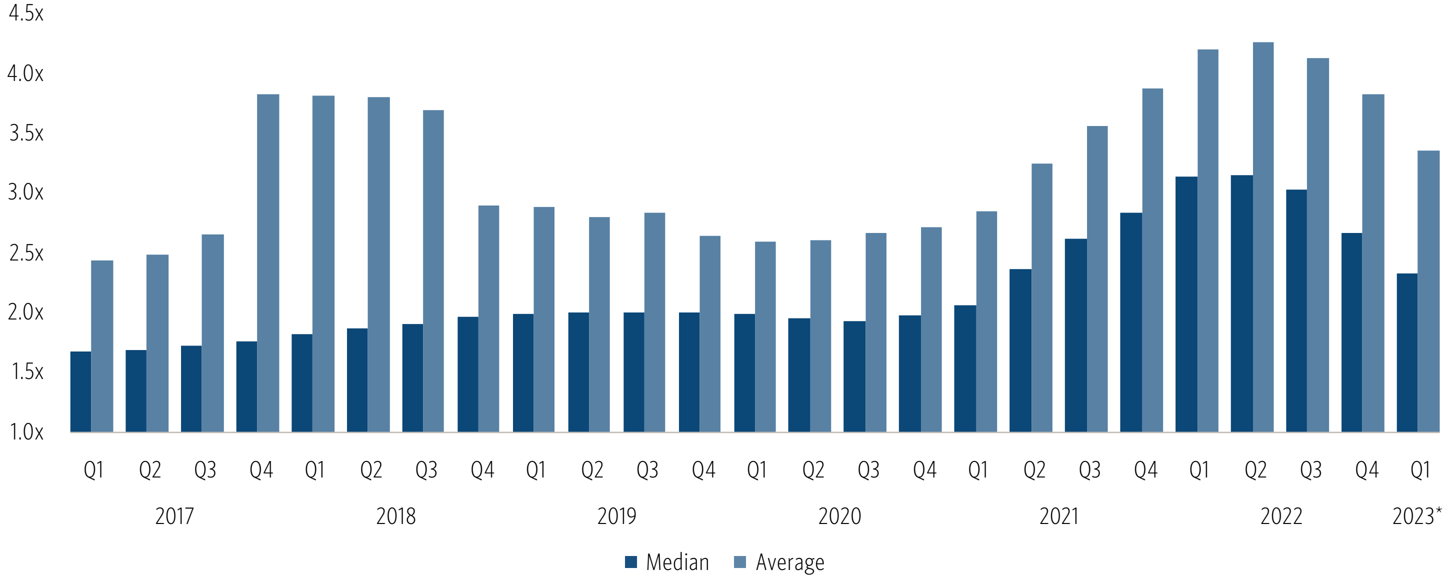
The median early-stage VC pre-money valuation has declined steadily since the highest point recorded, in Q1 2022. The figure settled at $38.2 million in Q1 2023, a 5.7% drop from the previous quarter and sitting at 63.1% of where it was in Q1 2022. The valuation decline is the result of GPs being more cautious and selective toward dealmaking amid a liquidity crunch.

The trends of GPs slowing the pace of capital deployment and prioritizing existing portfolio companies over handing out new term sheets, as well as a record high supply-and-demand ratio at the late stage, led to additional headwinds for early-stage startups. Many of these relatively more nascent companies have not developed strong financial metrics yet, thus making it extra challenging to justify a high valuation. Pressures from a lack of capital availability also trickle down to earlier stages of the venture ecosystem. Median and average step-ups have compressed to the lowest quarterly figures since the beginning of the COVID-19 pandemic, and the median time between rounds rose to 1.2 years, which is roughly two months longer than the 2022 annual figure. These increases are likely due to startups trying to adapt into a cost-effective structure, striking a balance between operating lean and achieving goals. The top quartile pre-money valuation ascended by 8.2% from Q4 2022, reaching $85.5 million. This upward trend further attests to a flight to quality. As investors are focused on ensuring the top performers of their portfolio have sufficient capital to reach key milestones, many are doubling down on the best-performing portfolio companies.

Median VVC (defined as the annual increase in valuation between rounds) slumped and settled at $16.1 million, a sizable 58.7% decline from the 2022 figure. In tandem, RVVC (annualized percent increase in valuation between rounds) slid to 41.9%, an outsized drop from 2022's 125.5%. Even if companies have achieved growth since their last financing rounds, investors are no longer competing against each other in oversubscribed rounds and bidding up the company's valuation. This market change, along with increased time between rounds, contributed to a slower pace of value creation in Q1.

Median step-up hits four-quarter slide

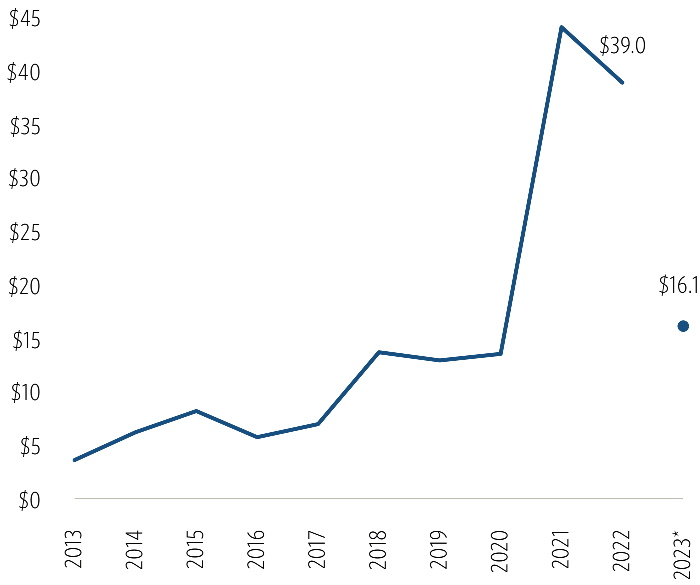
Rolling four-quarter median and average early-stage VC valuation step-up



Source: PitchBook • **Geography:** US
*As of March 31, 2023

Median early-stage velocity of value creation (VVC) adds just $16 million annually

Median early-stage VVC ($M) between rounds



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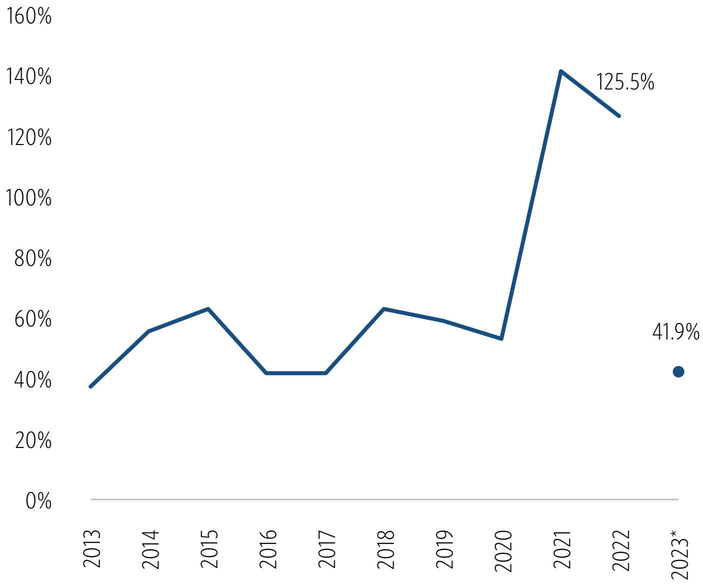
Median early-stage relative velocity of value creation (RVVC) lowest since 2017

Median early-stage RVVC between rounds



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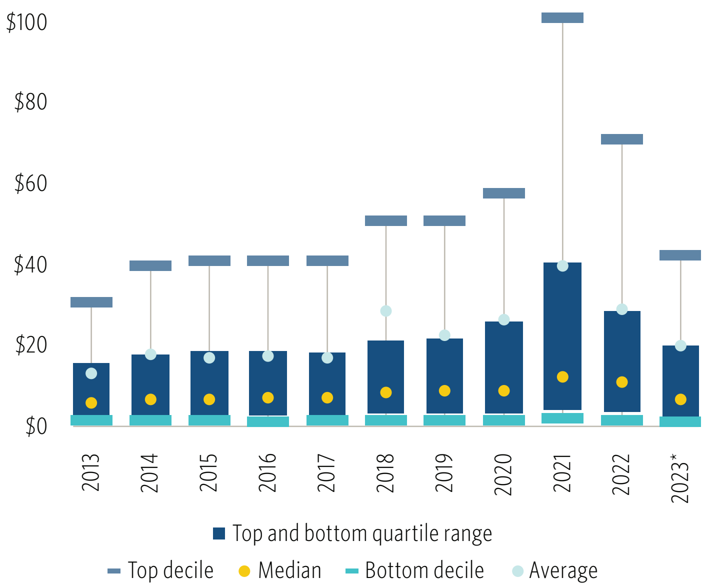
Late-stage VC valuations

Median late-stage deal value has fallen 40% YoY

Late-stage VC deal value ($M) dispersion



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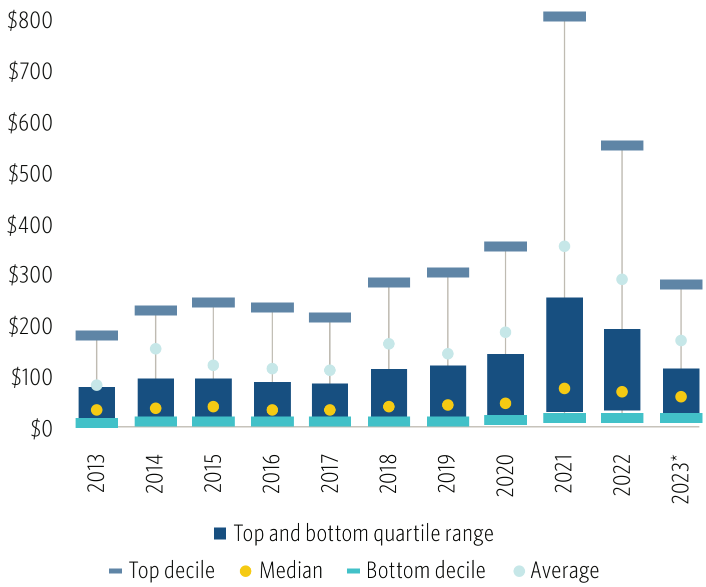
Top-decile valuation down 70% QoQ

Late-stage VC pre-money valuation ($M) dispersion



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Ongoing economic headwinds have significantly impacted the late-stage venture market, which has continued its descent from H2 2022. While the total number of late-stage deals completed in Q1 2023 was slightly higher than Q4 2022, the median deal size fell 25.0% to $6.0 million, which is the lowest figure observed since Q2 2017. The decrease in deal sizing speaks to the dearth of capital at the late stage; our data estimates the capital-demand-to-supply ratio at the late stage to be 3.24x, which means that for every one dollar of capital supplied by investors, there is $3.24 of capital sought by late-stage startups. This is especially concerning given that just one year ago, there was more capital available than was being demanded, due largely to a healthy population of sizable nontraditional investors putting capital into these enterprises.

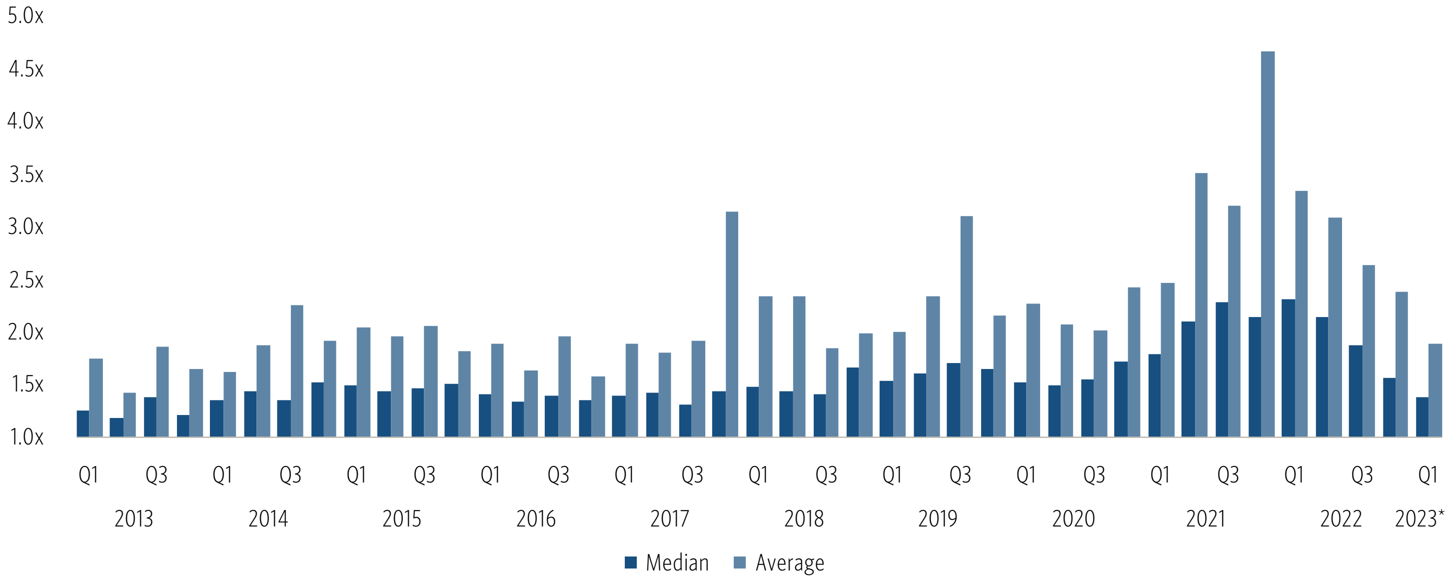
As the economy has slowed, so has the fervor of these nontraditional investors, which have exited the venture market en masse and taken their capital with them. Crossover investors, for example, participated in just 18.1% of all US VC deals in Q1, which is the lowest share observed since 2017.

Consequently, the exit of these investors and the subsequent capital crunch has substantially impacted valuations: The median late-stage valuation in Q1 fell to $55.0 million, an 8.3% decline from Q4. Additionally, the top-decile late-stage valuation in Q1 was $276.4 million—a whopping $623.6 million decline from the record high set in Q3 2021.

The current financing environment is no longer willing to uphold inflated valuations, and this affects not only founders and employees but also investors that are looking to realize value between rounds. The median late-stage VVC shrunk to $9.0 million in Q1, which is down from $19.8 million in 2022—falling below $10.0 million for the first time since 2018. We expect the valuation environment to worsen through the end of the year for many businesses at the top of the venture lifecycle as they lose the ability to wait out economic headwinds and inevitably return to a less startup-friendly fundraising market.

Average step-up below 2.0x for first time since 2018

Median and average late-stage VC valuation step-up by quarter



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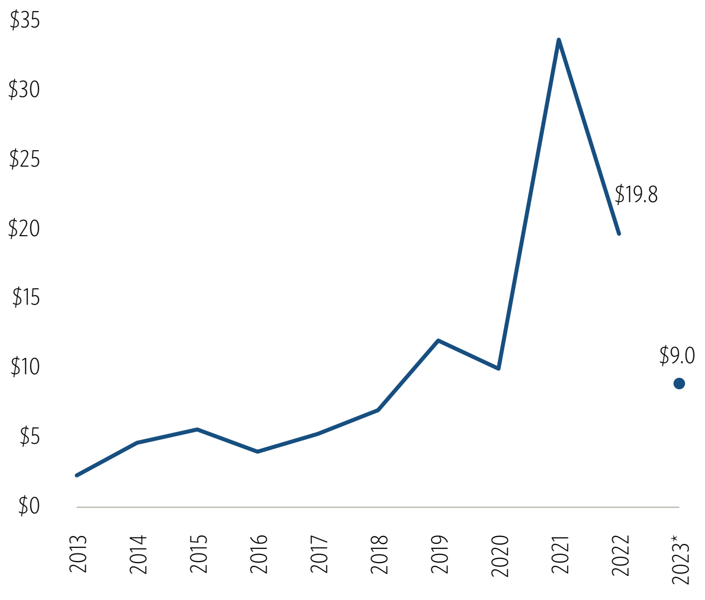
Late-stage VVC into single digits

Median late-stage VVC ($M) between rounds



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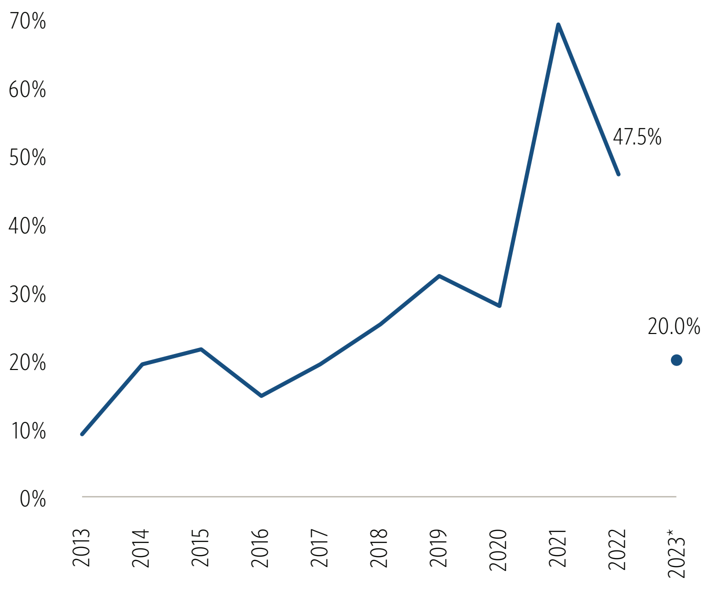
Lowest RVVC growth rate since 2017

Median late-stage RVVC between rounds



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A WORD FROM MORGAN STANLEY AT WORK

Exploring 409A valuations in the global private markets

Steve Liu

Executive Director, Co-Head of Valuation Services

Steve is responsible for leading the valuation practice and oversees client engagement, strategic partnerships, and business development activities to support the Global Private Markets group. Previously, Steve was the valuation practice leader at SVB Analytics. Prior to that, Steve worked with Deloitte and KPMG in New York and San Francisco, respectively, for more than a decade, managing both domestic and international clients that ranged from startups to Fortune 100 companies. Steve has a Master of Business Administration from New York University's Stern School of Business and master's and bachelor's degrees in engineering from The Cooper Union for the Advancement of Science and Art. He has received the designation Accredited Senior Appraiser in business valuation from the American Society of Appraisers and holds his Series 63 and 79 licenses from the Financial Industry Regulatory Authority.

What is Morgan Stanley at Work?

Morgan Stanley at Work provides workplace financial benefits that build financial confidence and foster loyalty—helping companies attract and retain talent. Our end-to-end offering spans Equity Solutions, Financial Wellness, and Retirement Solutions. Each benefit solution includes a powerful combination of modern technology, insightful support, and dedicated service that provides your employees with the knowledge and tools needed to help make the most of their benefits and achieve their life goals.

Our Global Equity Solutions help your company and employees make the most of your equity compensation plan so everyone feels invested in mutual accomplishment. We provide scalable end-to-end solutions that support your organization at any stage of growth.

How are you supporting private companies in the current climate?

Maintaining an accurate and audit-ready 409A valuation is important not only for complying with IRC 409A valuation requirements but also for making strategic decisions around equity. And as market conditions remain volatile, our team is helping private companies ranging from the early stage to pre-IPO stay current with their valuations, manage safe harbor requirements, and plan for their ongoing equity compensation needs.

We're also working with founders to provide education on the implications of rapidly changing private and public market trends and the potential impacts to their company valuations. As part of this, our team provides assistance with thinking through the possible implications of significant changes in company valuations and the accompanying cascading impacts, such as option repricing.

For startups still considering secondaries, our valuation services team can help plan and quantify the structure and impact to their 409A valuations. For later-stage companies, we provide support to help them navigate potential changes in their valuation methodology and remain transaction-ready for a future IPO or another exit event.

During times of uncertainty, what factors should venture-backed companies consider when it comes to 409A valuations?

As tempting as it may be, management may want to avoid attempting to overengineer maintainable earnings. The International Valuation Standards Council notes that "[t]he objective [of the valuation] is not to stress test a valuation to an extreme case."[1] As much as short-term volatility can impact a company's valuation, management might consider adopting a more holistic perspective that considers the stage of development of the business, financial fundamentals, sector-specific market dynamics, and the time horizon to exit. Management may also want to keep in mind that a significant decrease in a company's valuation can potentially start a conversation around stock option repricing. Because repricing is typically a one-time event, this decision needs to make sense for both the short term and the long term.

1: "Valuation Uncertainty at Times of Market Unrest," International Valuation Standards Council, April 20, 2020.

For companies that are not considering repricing, it can be important to weigh the pros and cons from the perspective of its option holders. Employees may become frustrated or feel differently about their equity if it no longer represents an upside to them. Furthermore, option holders that must exercise their options while the strike price remains higher than the current 409A valuation may be doing so at a loss or be forced to abandon their shares by never exercising them.

Lastly, management may want to consider that the overall message to employees is not lost. A 409A valuation can be a chance to communicate to employees the value of their equity compensation and remind them why they joined the company in the first place. This can be important not only for recruiting talent but also for retaining it. So, as much as a 409A valuation is a number at the end of the day, more importantly, it may be an opportunity to share with employees an important narrative on behalf of the company that helps create a sense of ownership, especially during times of market uncertainty.

What are some trends you are seeing within 409A valuations?

With a safe harbor of 12 months, 409A valuations are typically what we call a lagging indicator. What that means is that while a company's past 409A valuation may have been based on a healthy step-up in pricing from a recent round of capital, the funding and the market environment may have changed in the past year. At Morgan Stanley at Work, we've seen valuations recalibrate to new market norms and repricing become a common refrain. However, it should be noted that not every company is affected by market conditions in the same way. Despite the market volatility today, there can be notable exceptions where startups continue to raise capital and maintain sound financial KPIs that result in higher valuations.

For companies that completed secondaries or tender offers, which were accounted for in prior 409A valuations, we've seen pricing recalibration that extends beyond the 409A valuation. For startups that are still considering strategic secondaries sales, there can be greater interest in exploring liquidity options outside the traditional avenues.

Given the amount of volatility happening in the global markets, what can private companies do to manage their ongoing 409A valuation needs?

For startups in particular, the mantra today has become "cut burn and extend runway." In other words, the focus has turned toward cash flow and ensuring the durability of the business given the current funding environment. With uncertainty over the company's next funding round or financing event (or where it comes from), financial metrics can be more important than ever as drivers for a business's valuation. This contrasts reliance on pricing from historical capital raises that are arguably obsolete.

Next, the annual cadence of 409A valuations was previously in sync with the 12-month safe harbor period and normal market conditions; however, these are anything but normal times. Remember, it doesn't cost anything to have a discussion with your 409A valuation provider to revisit your company's valuation, especially if you may be contemplating a significant option grant, repricing, or secondary/tender offer.

Lastly, for startups that have deferred their private-to-public plans, consider that 409A valuations and related activities (such as secondaries and tender offers) within three years of an IPO are subject to public disclosure. So, as much as current market conditions are rife with volatility, it may be prudent to think ahead and proactively prepare for those events.

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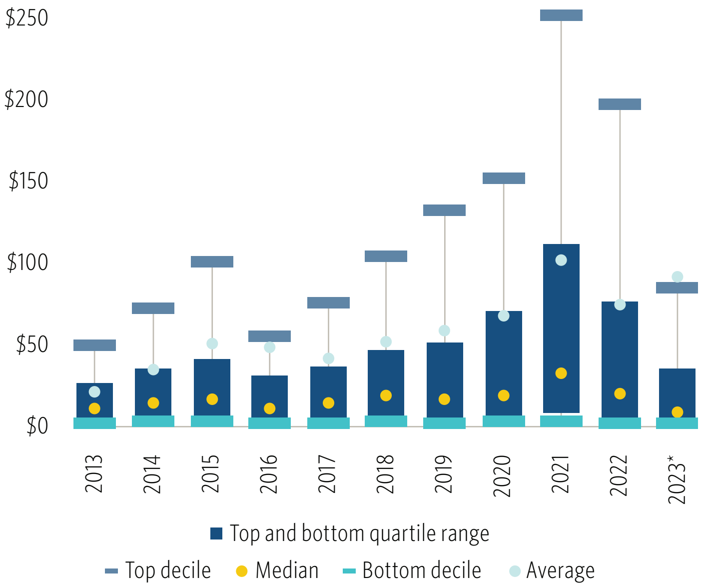
Venture-growth valuations

Median deal size nearly 50% lower than Q4

Venture-growth deal value ($M) dispersion



Source: PitchBook • **Geography:** US
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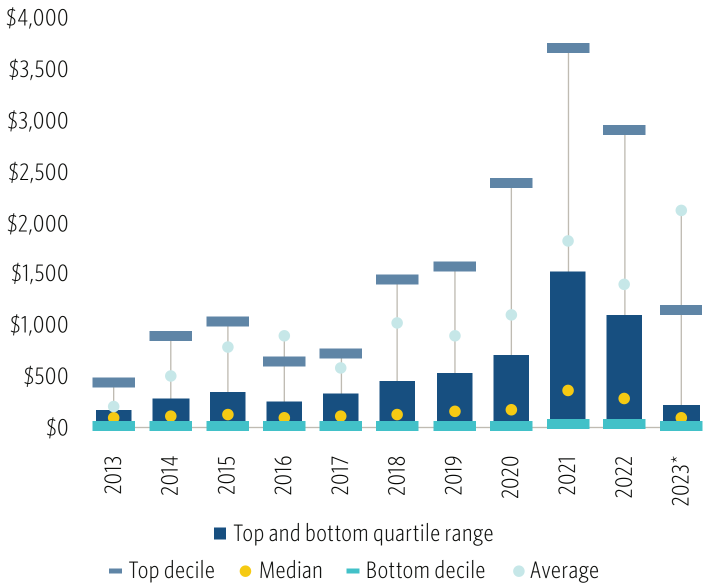
Median pre-money valuation lowest since Q1 2018

Venture-growth pre-money valuation ($M) dispersion



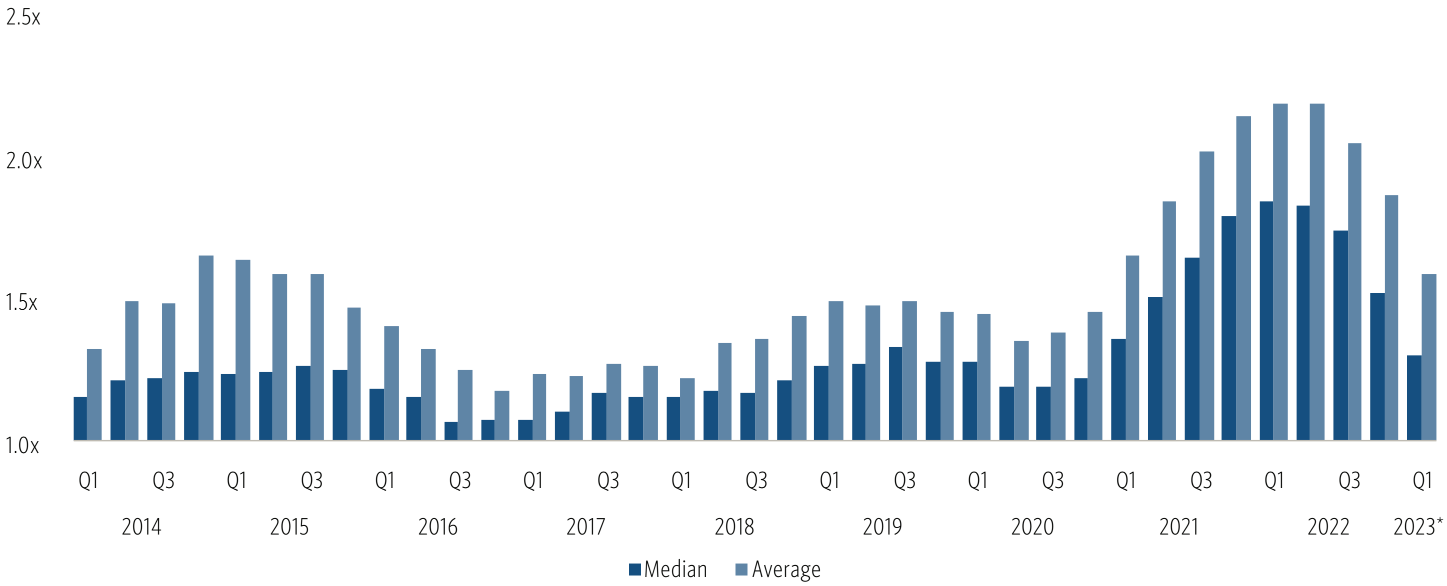
Source: PitchBook • **Geography:** US
*As of March 31, 2023

The lack of viable paths to liquidity, the nontraditional investor pullback, and the renewed focus on lean, capital-efficient business models have continued to pressure venture-growth-stage startups. In Q1, the median pre-money valuation fell to $90.0 million, representing a 74.6% decline from the 2021 full-year record high of $355.0 million. For the first time since Q1 2018, quarterly pre-money valuations have fallen below $100 million. Investor confidence in venture-growth-stage investments has been shaken as public and private valuations continue to reconcile. Investors are requiring larger equity positions to mitigate the increased risks of the current VC environment, thus leading to compressed valuations. This in turn has dramatically impacted valuation step-ups such that Q1's rolling four-quarter median step-up fell to 1.3x from its decade-high of 1.8x. The parabolic appearance of the rolling four-quarter step-ups from Q2 2020 through Q1 2023 coinciding with the VC market's valuation swell and compression suggests that step-up multiples will continue to fall through the end of the year back to low-growth figures.

Accompanying the decline in valuations and step-up multiples are venture-growth-stage deal sizes, which saw a Q1 median of $7.0 million, representing a 47.8% decrease from the Q4 2022 median of $13.4 million. Not only did the median deal size fall, but the top-decile deal size also fell below $100.0 million for the first time since Q1 2018. The shrinking deal sizes suggest several contributing factors: the diminished supply of capital historically made available by the participation of nontraditional investors; the interest of startup founders to minimize equity dilution by raising smaller amounts of capital at flat or nominally higher valuations; and the consideration of venture debt as a complementary source of financing to further extend cash runway without large impacts to the cap table. A prime example of this is Good Eggs, a fresh grocery delivery company, which reportedly took a 94% valuation haircut to secure $7.0 million in lifeline capital in Q1 2023. While this is an extreme case, we expect the frequency of down rounds to pick up among the venture-growth stage through the end of the year.

Step-ups show little growth for companies

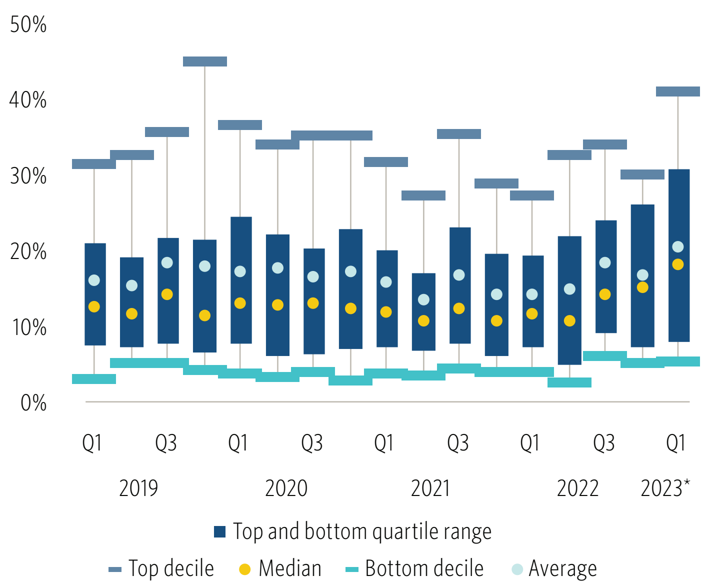
Rolling four-quarter median and average venture-growth valuation step-up



Source: PitchBook • **Geography:** US
*As of March 31, 2023

Investors requiring larger stakes

Venture growth share acquired dispersion by quarter



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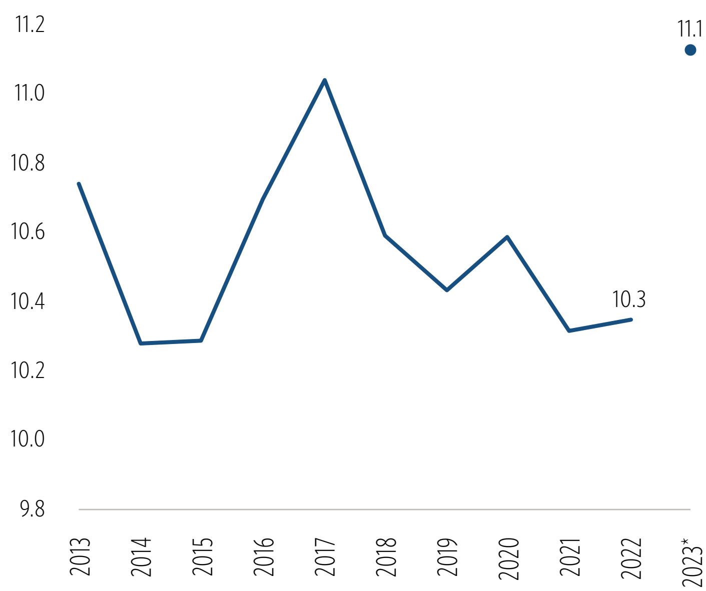
Lack of liquidity trapping companies

Median time (years) from founding for venture-growth companies



Source: PitchBook • **Geography:** US
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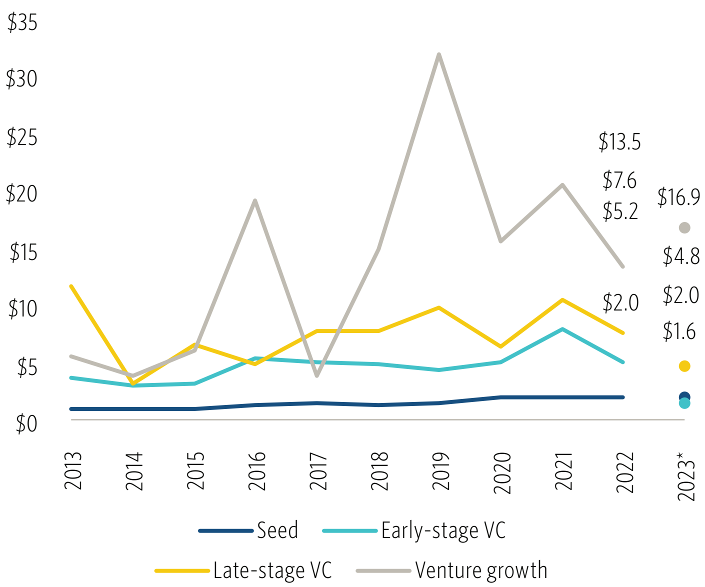
Agricultural technology (agtech)

Median venture-growth deal sizes see uplift in Q1

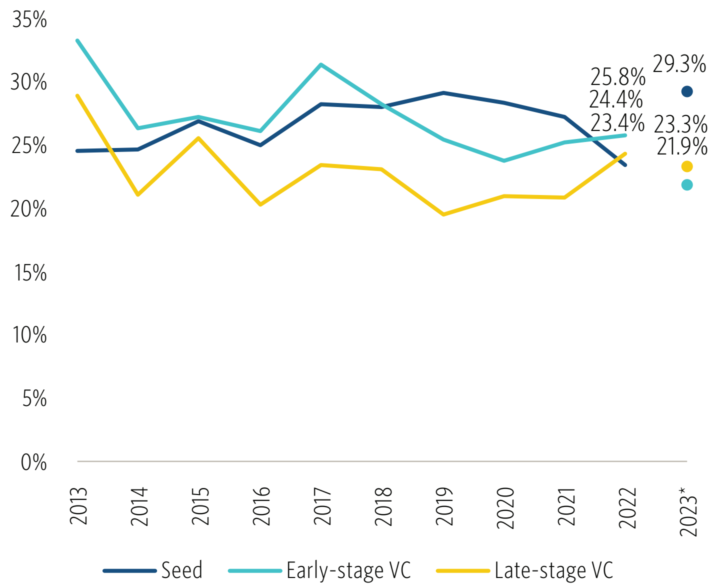
Median agtech VC deal value ($M) by stage



Source: PitchBook • **Geography:** US
*As of March 31, 2023
Note: Low data count for Q1 2023.

Investors seek larger equity positions in seed-stage startups

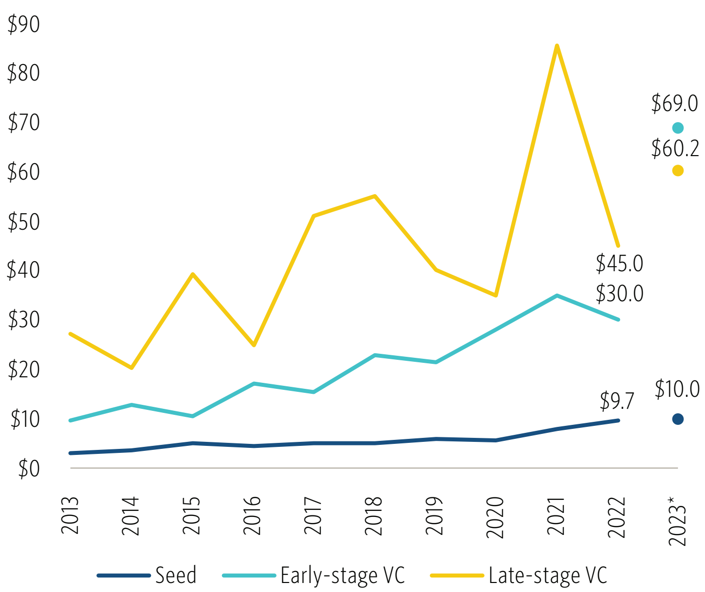
Median agtech VC share acquired by stage



Source: PitchBook • **Geography:** US
*As of March 31, 2023
Note: Low data count for Q1 2023.

Median early-stage valuations surpass late-stage

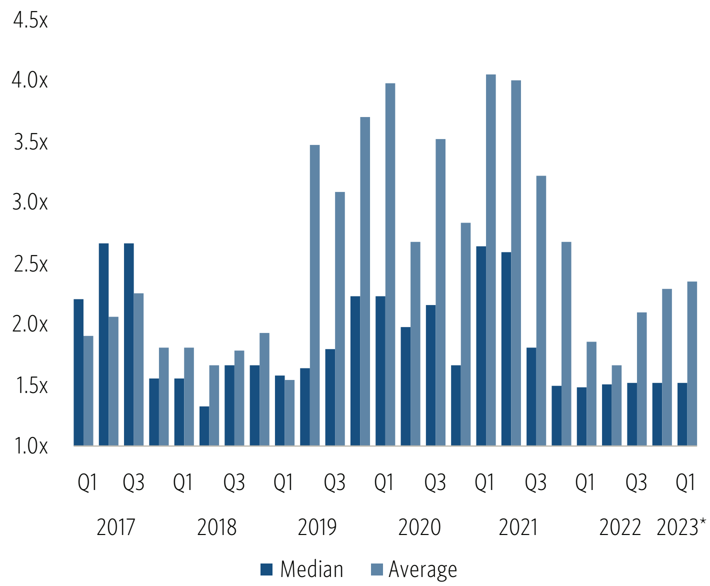
Median agtech VC pre-money valuation ($M) by stage



Source: PitchBook • **Geography:** US
*As of March 31, 2023
Note: Low data count for Q1 2023.

Median seed-stage step-ups on par with prior five quarters

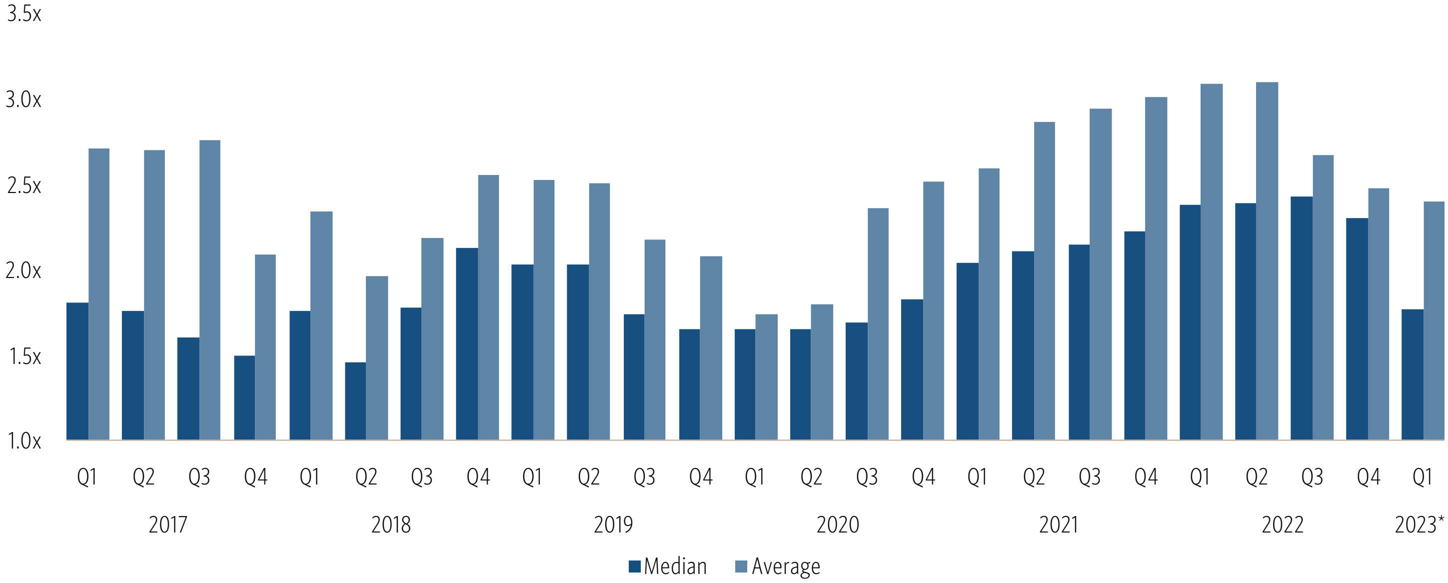
Rolling four-quarter median and average agtech seed VC valuation step-up



Source: PitchBook • **Geography:** US
*As of March 31, 2023

Early-stage step-ups continue their descent

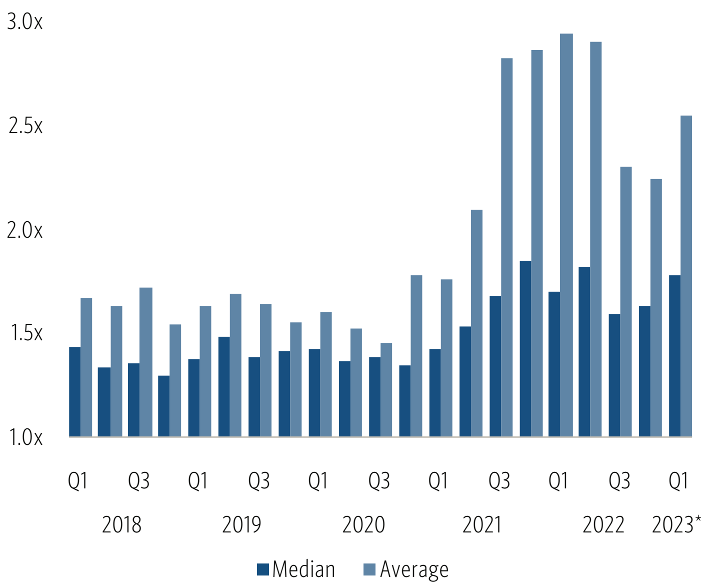
Rolling four-quarter median and average agtech early-stage VC valuation step-up



Source: PitchBook • **Geography:** US
*As of March 31, 2023

Q1 median late-stage step-ups show modest increase from prior quarter

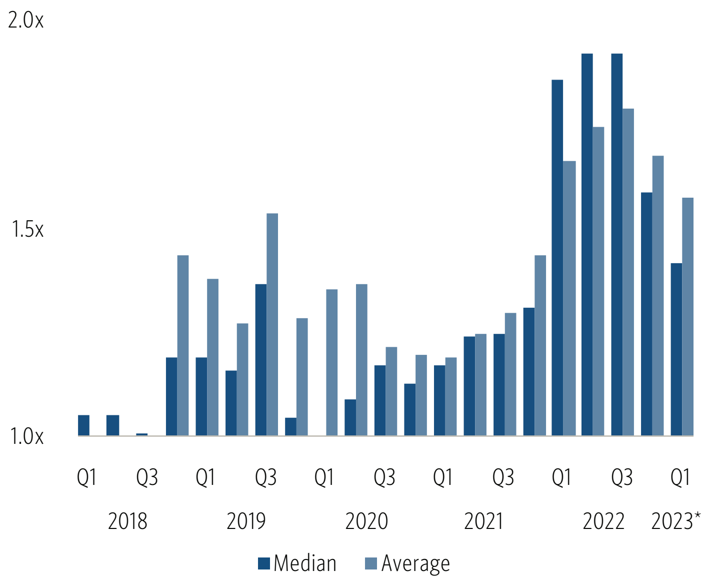
Rolling four-quarter median and average agtech late-stage VC valuation step-up



Source: PitchBook • **Geography:** US
*As of March 31, 2023

Venture-growth stage step-ups remain above 2021 figures

Rolling four-quarter median and average agtech venture-growth valuation step-up

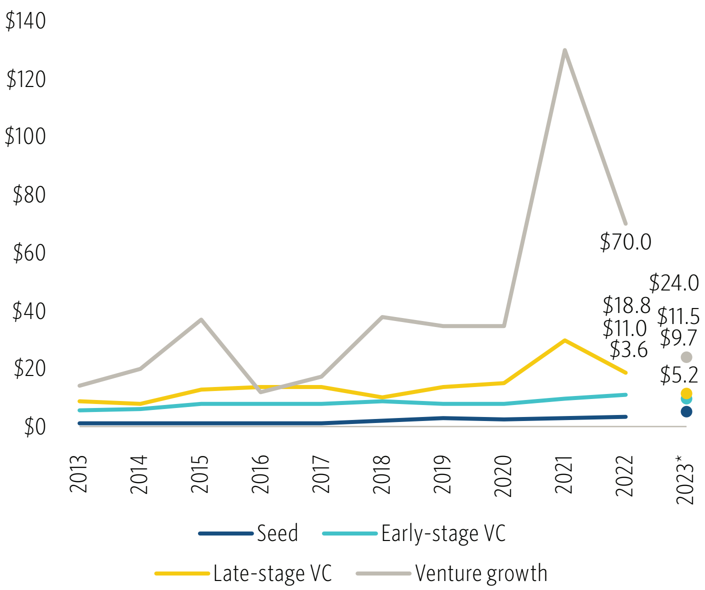


Source: PitchBook • **Geography:** US
*As of March 31, 2023

Information security (infosec)

VC mega-deals evaporating as unicorns pursue venture debt

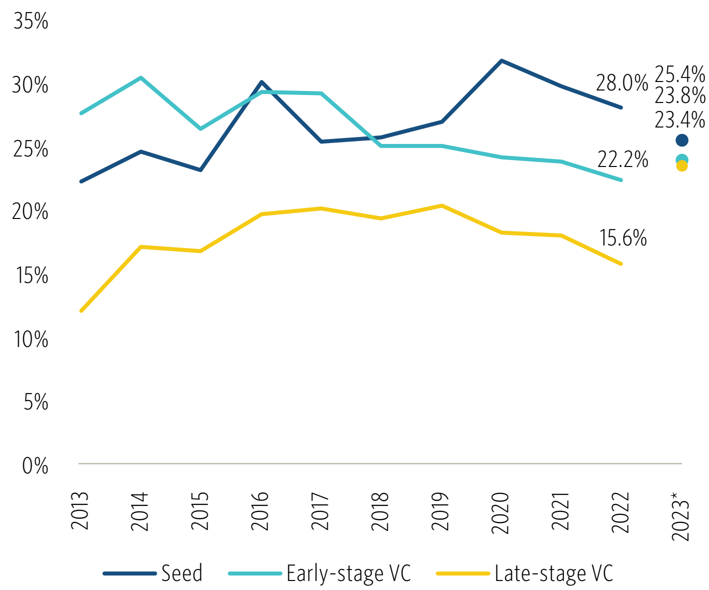
Median infosec VC deal value ($M) by stage



Source: PitchBook • **Geography:** US
*As of March 31, 2023
Note: Low data count for Q1 2023.

Seed rounds retain founder-friendly dilution, while investors benefit from supporting late-stage companies

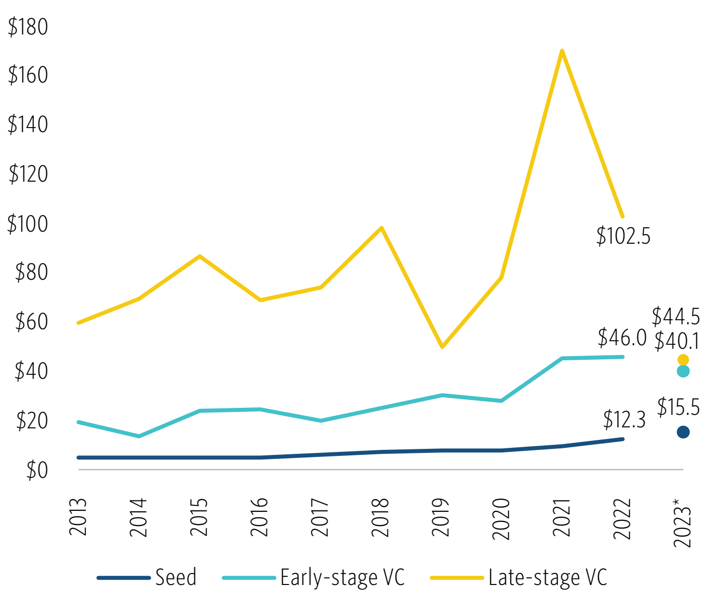
Median infosec VC share acquired by stage



Source: PitchBook • **Geography:** US
*As of March 31, 2023
Note: Low data count for Q1 2023.

Early- and late-stage valuations converging given limited support from venture-growth investors

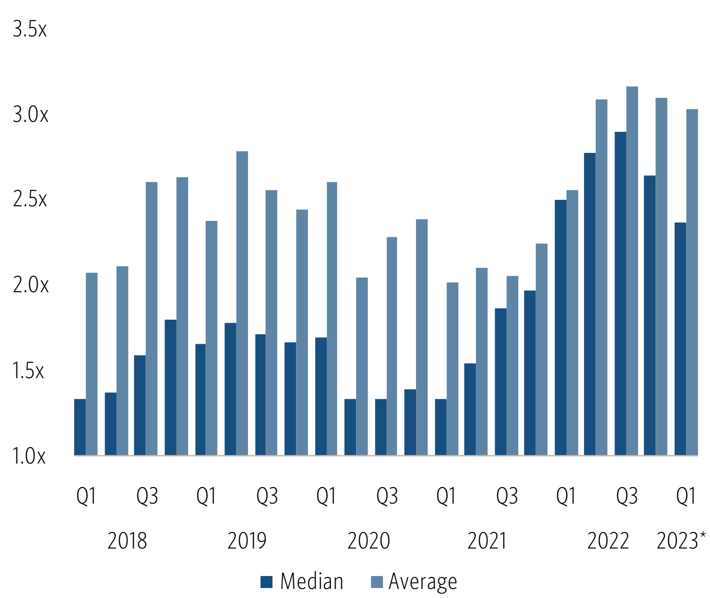
Median infosec VC pre-money valuation ($M) by stage



Source: PitchBook • **Geography:** US
*As of March 31, 2023
Note: Low data count for Q1 2023.

Step-ups remain consistently higher than market medians

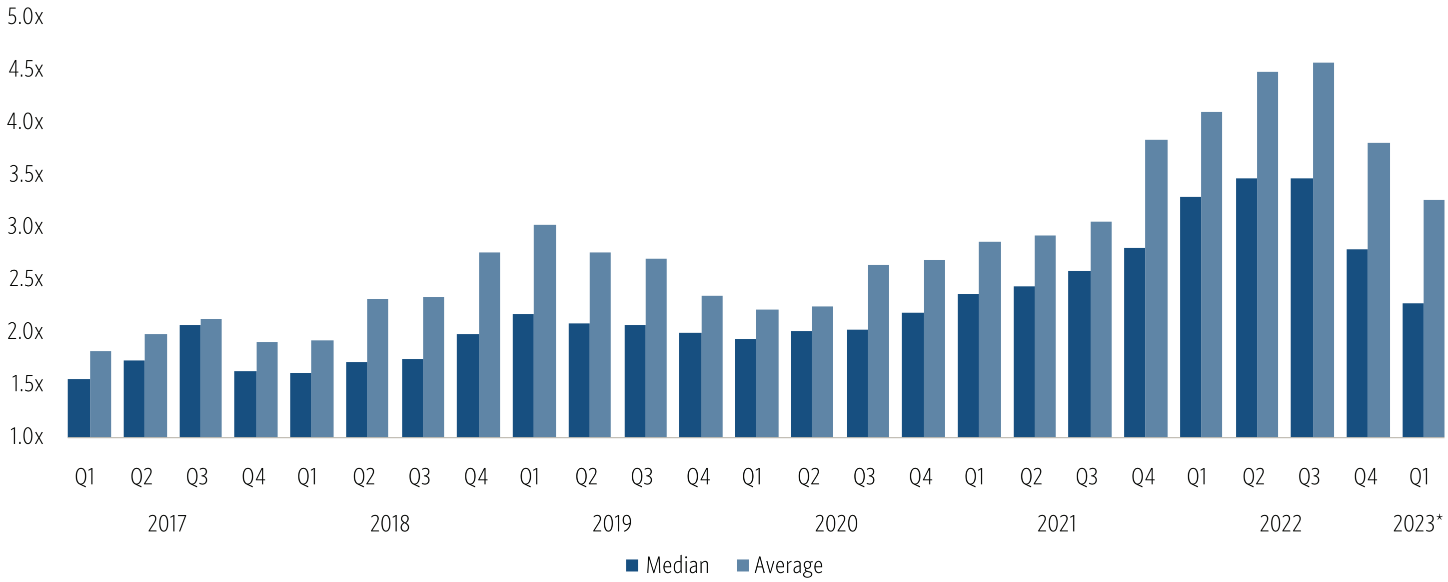
Rolling four-quarter median and average infosec seed VC valuation step-up



Source: PitchBook • **Geography:** US
*As of March 31, 2023

Infosec early-stage valuation step-ups fall below market norms, showing barriers to entry

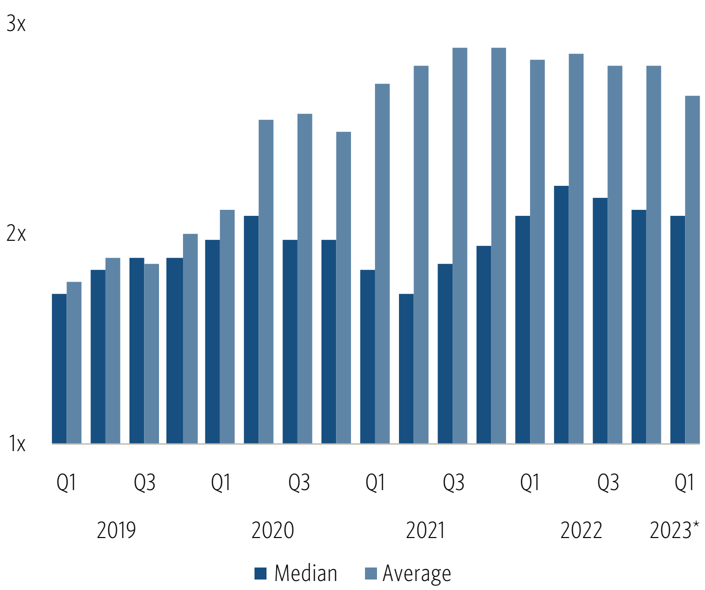
Rolling four-quarter median and average infosec early-stage VC valuation step-up



Source: PitchBook • **Geography:** US
*As of March 31, 2023

Infosec late-stage valuation step-ups remain resilient

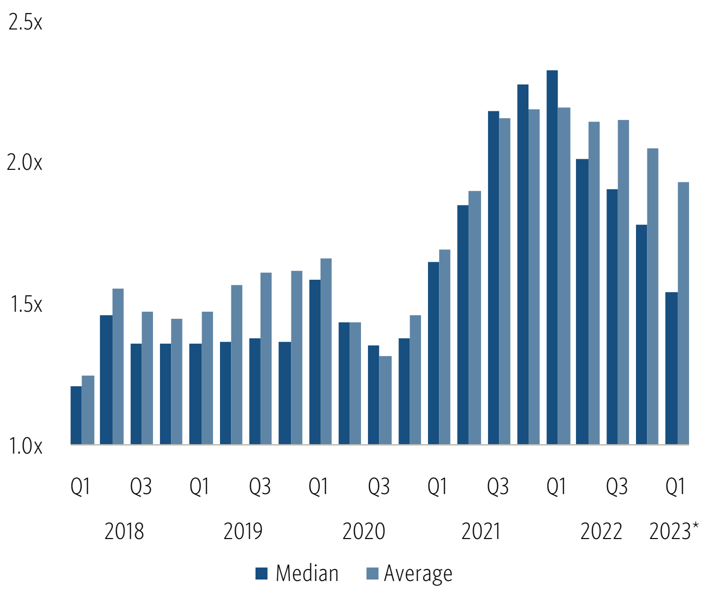
Rolling four-quarter median and average infosec late-stage VC valuation step-up



Source: PitchBook • **Geography:** US
*As of March 31, 2023

Infosec venture-growth valuation step-ups remain above market norms during downturn

Rolling four-quarter median and average infosec venture-growth valuation step-up

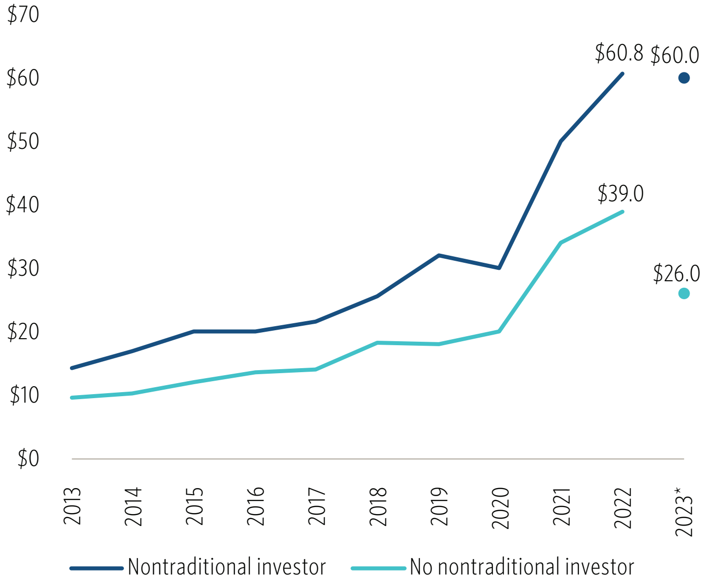


Source: PitchBook • **Geography:** US
*As of March 31, 2023

Nontraditional investors

Early-stage valuations of deals with NTI participation roughly flat

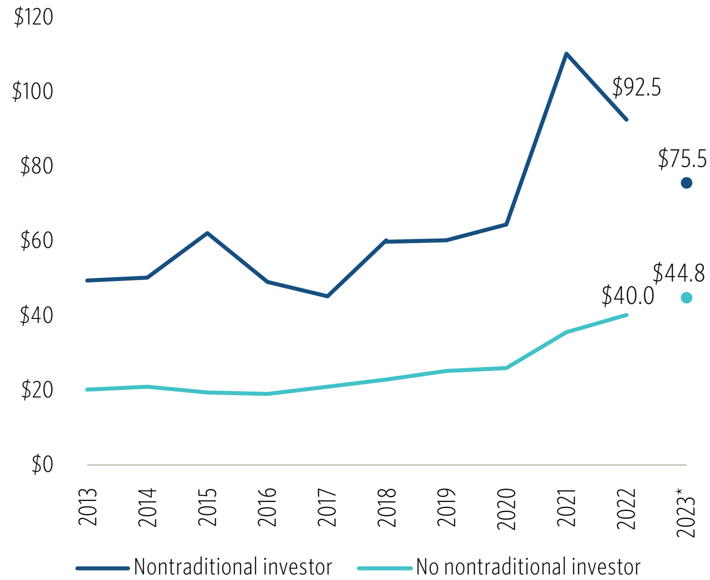
Median early-stage VC pre-money valuation ($M) with nontraditional investor participation



Source: PitchBook • **Geography:** US
*As of March 31, 2023

Median late-stage valuation of deals with NTI falls to $75.5 million

Median late-stage VC pre-money valuation ($M) with nontraditional investor participation



Source: PitchBook • **Geography:** US
*As of March 31, 2023

Nontraditional investors have continued to pull back from VC as result of a lack of liquidity. The lone exception to this pullback are CVCs, which typically invest earlier in the venture capital lifecycle and are therefore less exposed to the aforementioned factors, thus leading them to set a record participation rate on a deal count basis of 26.5% in Q1 2023. CVCs, often incentivized by strategic investments over financial returns, have focused on seed- and early-stage deals, with 60.2% of completed financings occurring at these stages YTD.

Examining the deal metrics associated with the broader nontraditional investor group's participation shows average pre-money valuations have declined across all stages, but most significantly in the late and venture-growth stages, which have more exposure to public market volatility. At the same time, the average amount of equity acquired increased across all stages by 2% to 5%. Nontraditional investors, especially those participating with financial returns in mind, compensate for increased risks in the market by requiring a larger equity share and in turn compressing valuations. As startups become more capital starved and the bargaining power of nontraditional investors grows, we expect nontraditional investors to demand more equity and cause valuations to slide further.

Pullback aside, nontraditional investors play a crucial role in adding much-needed capital to the US VC ecosystem, thus bolstering deal metrics. The Q1 2023 median seed-stage deal size with nontraditional investor participation was $4.6 million; without nontraditional investor participation, it was just $1.4 million. Similarly, the Q1 median late-stage pre-money valuation with nontraditional investor participation was $75.5 million, versus just $44.8 million without. Deal metrics are larger with nontraditional investor participation for several reasons, including the need to participate in larger rounds to effectively deploy capital from their balance sheets, co-investing alongside investors with more experience in evaluating deals, and leveraging their brand name to attract more capital and achieve higher valuation premiums. Startups that receive capital from nontraditional investors will likely be able to continue raising deal sizes and justify valuations above the broader market median.

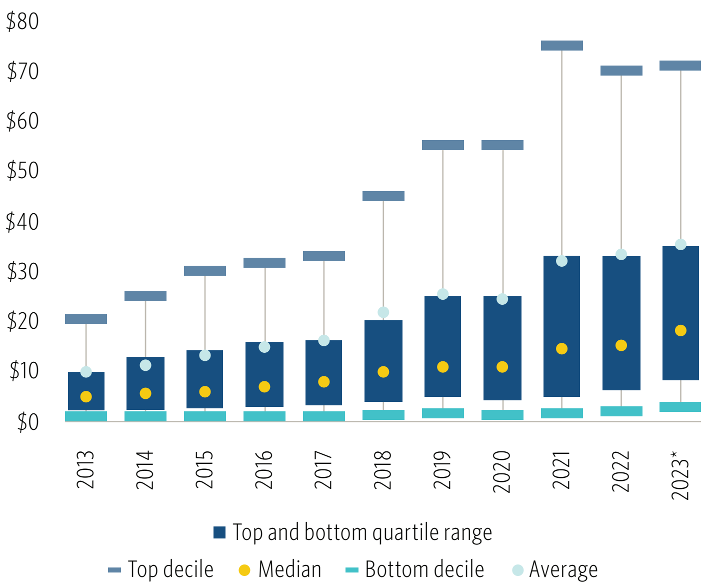
Nontraditional investors continue to pull away from VC

VC deal activity with nontraditional investor participation by quarter

Source: PitchBook • **Geography:** US
*As of March 31, 2023

Median and average early-stage NTI deal values surpassed 2021 levels

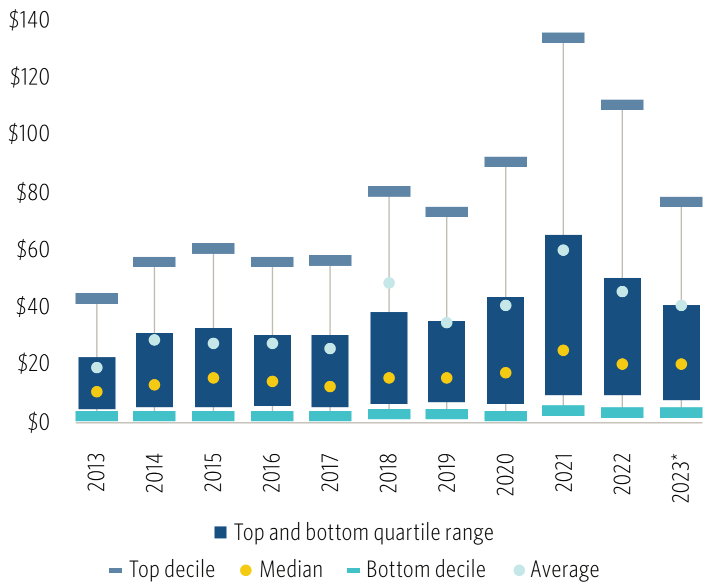
Early-stage VC deal value ($M) dispersion with nontraditional investor participation



Source: PitchBook • **Geography:** US
*As of March 31, 2023

Average late-stage NTI deal value fell 10.5% YoY

Late-stage VC deal value ($M) dispersion with nontraditional investor participation

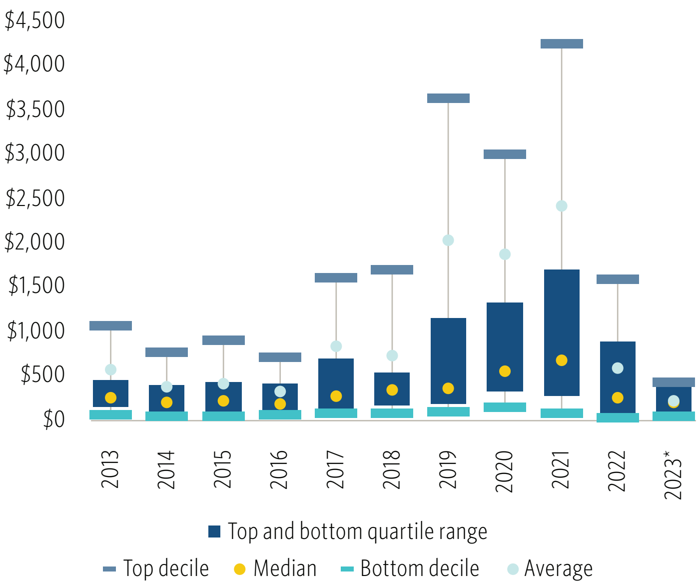


Source: PitchBook • **Geography:** US
*As of March 31, 2023

Liquidity

Average public listing just $215 million initial valuation

Valuation ($M) at exit via public listing dispersion

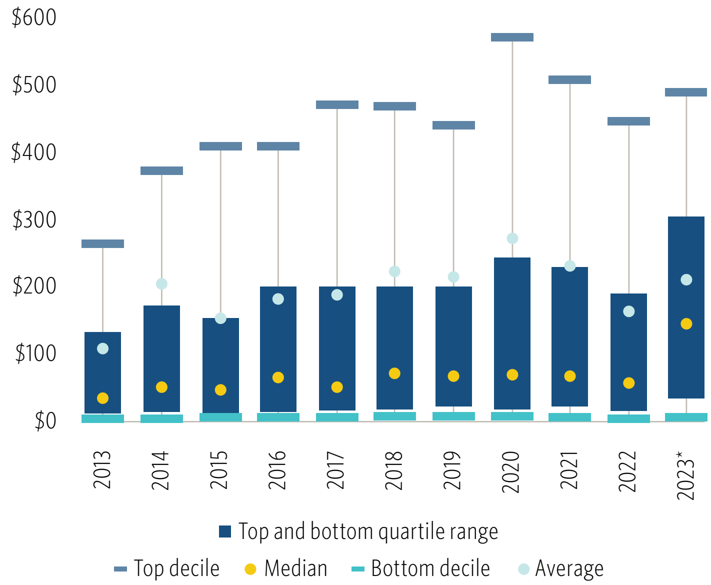


Source: PitchBook • **Geography:** US
*As of March 31, 2023

Notes: "Valuation at exit" for IPO represents pre-money valuation. "Public listing" indicates that a company exited via an IPO, direct listing, or reverse merger.

Average acquisition rises, but data counts low

Valuation ($M) at exit via acquisition dispersion



Source: PitchBook • **Geography:** US
*As of March 31, 2023

Despite a host of high-quality companies queuing up for a public debut,[2] the IPO market remains shut due to elevated interest rates and low investor confidence. Q1 recorded merely 20 public exits, including eight IPOs. The total exit count showed modest improvements from previous quarters and is on par with early 2022 levels, driven primarily by M&A activity. Many of these cash-burning, mature startups are trapped in a capital availability crunch and will likely have to risk raising a flat or down round, explore debt options, or, in an ideal case, achieve positive cash flow to wait out a hostile financing environment.

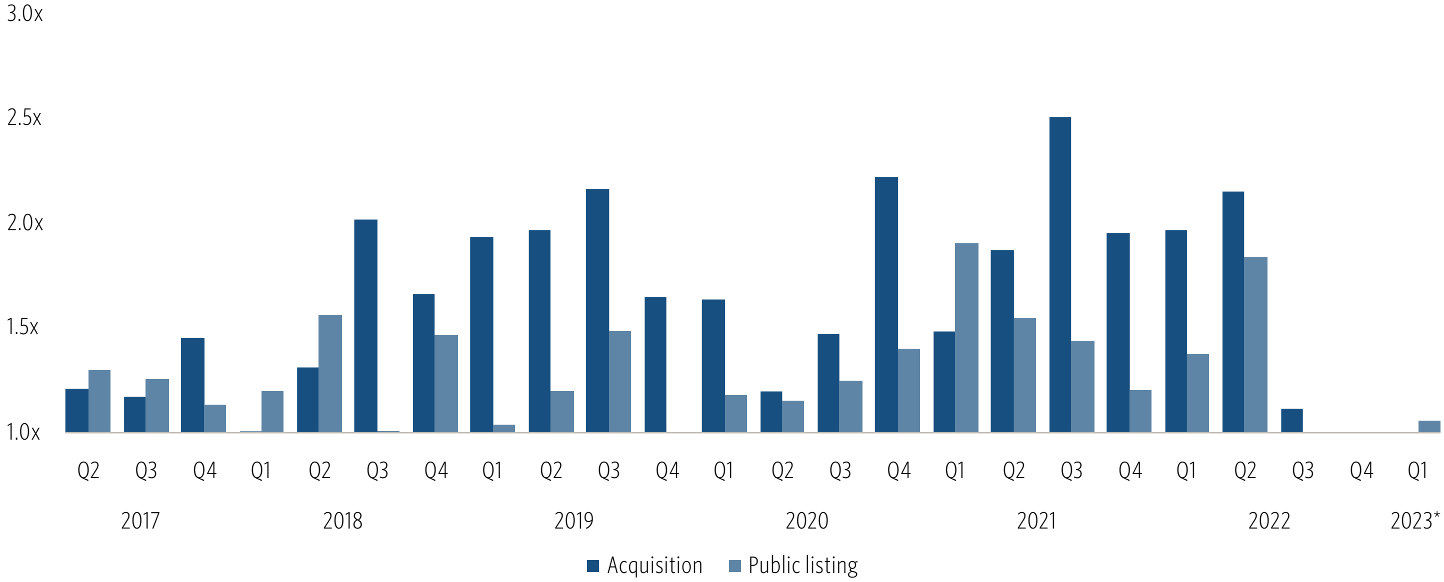
The median public listing VC exit valuation jumped to $185.9 million in Q1, up 42.3% from the previous quarter. Despite this substantial quarterly increase, the figure is only a fraction of the lofty valuations recorded in 2021 and more closely resembles 2018 levels. Among all public exits completed in Q1, half were healthcare deals, and all four of the tech exits were reverse mergers. Historically, tech IPOs tend to generate outsized exit value and returns for the market. We expect to see a leap in exit valuation when the public market is ready to host tech unicorns, though this remains distant. Anecdotally, some investors believe the IPO market is unlikely to reopen later this year, and people might have to wait till 2024. With a return of investor demand, a large backlog of startups with solid business models, healthy financials, and sustainable growth will be able to capitalize on the opportunity to access the public market.

Private market valuation declines present an opportunity for corporations with abundant cash reserves to acquire startups with a high level of synergies. Not knowing when the market will hit rock bottom, some founders may look to sell their businesses at a discount to return liquidity to cap table shareholders, as well as for peace of mind. Anecdotally, M&A activity for privately held companies has ticked up in the first two quarters of 2023, albeit through relatively small transactions.

2: As of February 28, 2023, 219 companies are estimated to be in the IPO backlog, as discussed in our Q1 2023 Quantitative Perspectives: Putting the Pieces Back Together.

Few large exits to generate returns

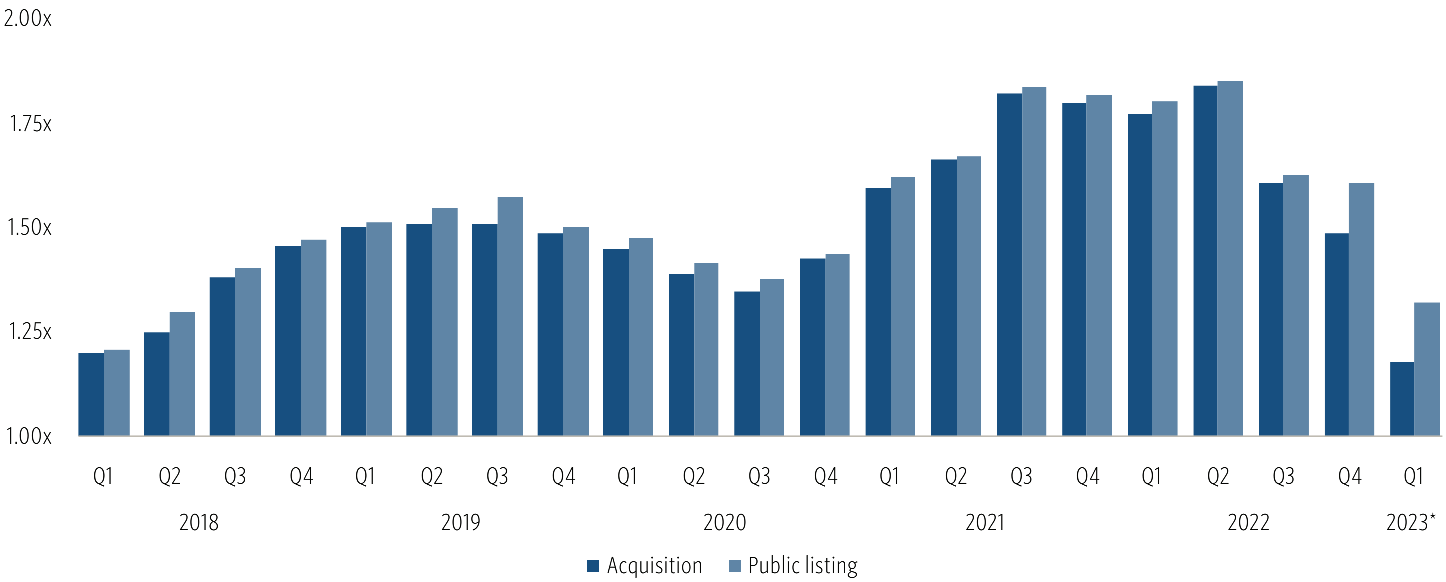
Quarterly median valuation step-up at exit by type



Source: PitchBook • **Geography:** US
*As of March 31, 2023
Note: "Public listing" indicates that a company exited via an IPO, direct listing, or reverse merger.

Median step-up at exit remained relatively unchanged

Rolling four-quarter median step-up at exit by type

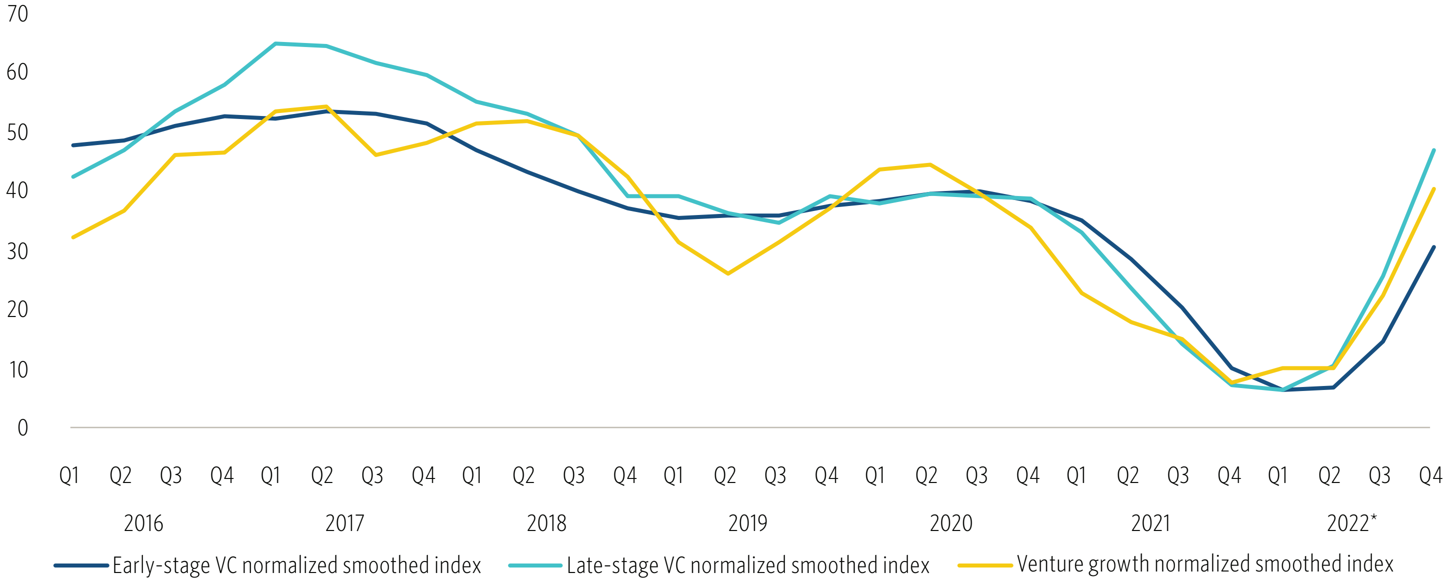


Source: PitchBook • **Geography:** US
*As of March 31, 2023
Note: "Public listing" indicates that a company exited via an IPO, direct listing, or reverse merger.

Deal terms

Venture market quickly becoming more investor-friendly

VC Dealmaking Indicator by quarter



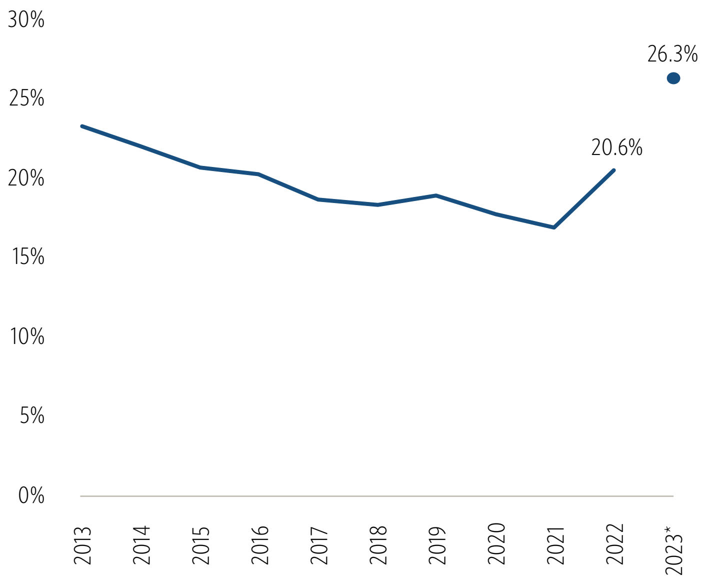
Source: PitchBook • **Geography:** US
*As of December 31, 2022

Our VC Dealmaking Indicator shows that the US venture market has strongly favored investors through the first quarter of the year. In fact, we estimate that Q1 2023 marks the most investor-friendly market environment observed in nearly 10 years. Given the current economic environment and ongoing volatility, more structured equity deals favoring investors are to be expected. Our data reveals an uptick in the occurrence of downside protections being negotiated in term sheets, and we anticipate this trend to increase in coming quarters as investors look to de-risk future investments.

Over the past three quarters, there has been a growing trend of investors securing cumulative dividends, which guarantees them accrued dividend payments. This upward trend reflects heightened investor interest in securing economic benefits from their investments, even in situations wherein the outcome may not be optimal. Through Q1, our data shows that the proportion of cumulative dividends as a share of all dividends is 26.3%—the highest percentage we've observed in over a decade. Participating shares have also become increasingly frequent, indicating a growing demand from investors to negotiate additional consideration beyond the standard liquidation preference payout.

Deals with cumulative dividends jump to 26.3%

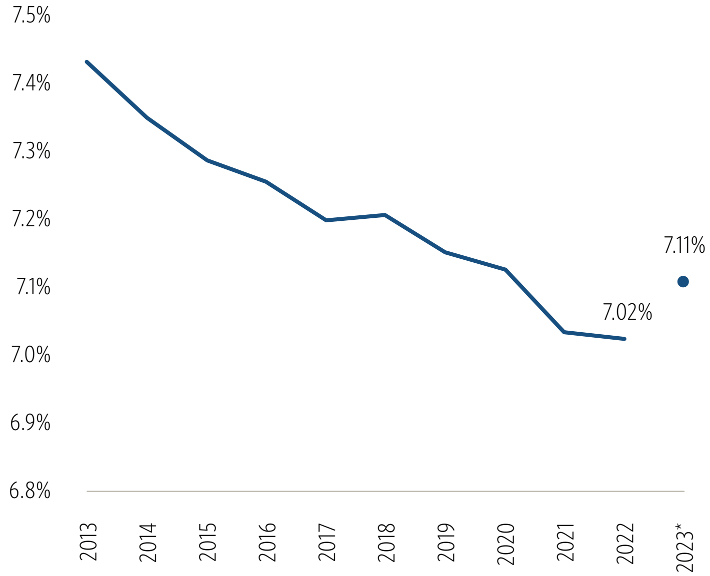
Deals with cumulative dividends as share of all VC deals



Source: PitchBook • **Geography:** US
*As of March 31, 2023

Average dividend increased to three-year high

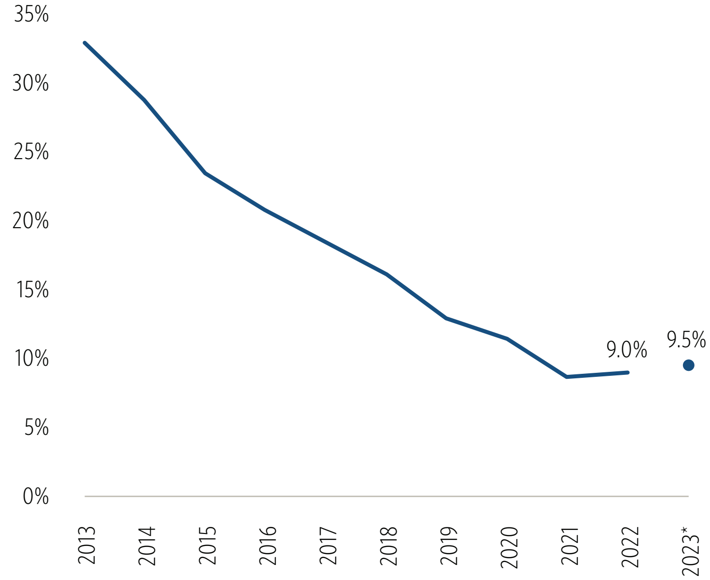
Average dividend



Source: PitchBook • **Geography:** US
*As of March 31, 2023

Participating shares increase in proportion

Deals with liquidation participation as a share of all VC deals

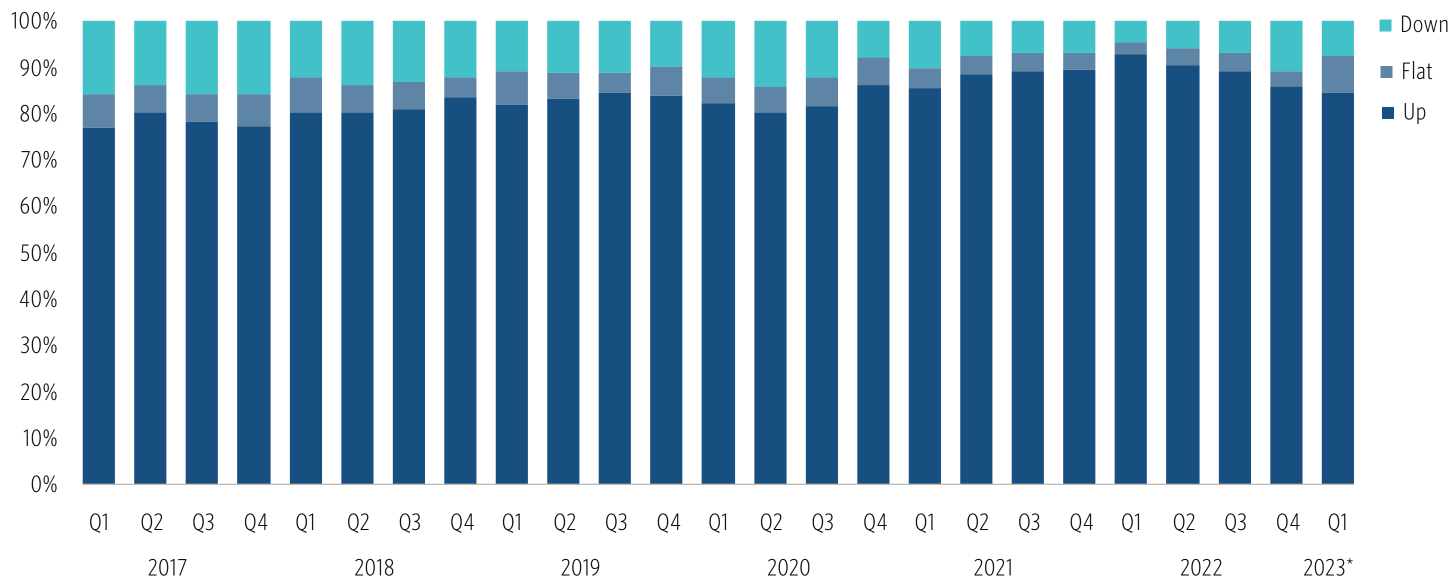


Source: PitchBook • **Geography:** US
*As of March 31, 2023

The proportion of flat and down rounds as a share of all rounds completed grew for the fourth consecutive quarter, representing 7.5% of all rounds in Q1 2023, which is roughly 5.7% higher than Q1 2022. While elevated, this is likely the calm before the storm as many startups that face the risk of raising equity capital at a stagnant or reduced valuation are choosing to delay their return to market in hopes that the valuation environment will become more hospitable. Given that many of these businesses will not be able to wait out the market, we expect the percentage of flat and down rounds to increase substantially in the coming quarters.

Down rounds start to climb

Share of VC deals by up, flat, or down rounds by quarter



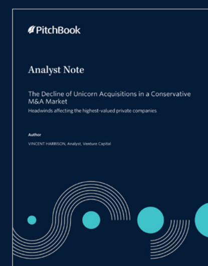
Source: PitchBook • **Geography:** US
*As of March 31, 2023

Additional research

Private markets

Q1 2023 PitchBook-NVCA Venture Monitor

Download the report here



Q2 2023 Analyst Note: The Decline of Unicorn Acquisitions in a Conservative M&A Market

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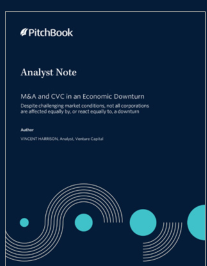

Q1 2023 Analyst Note: M&A and CVC in an Economic Downturn

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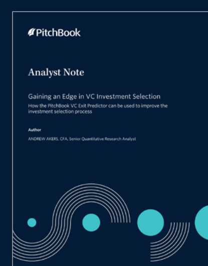

Q1 2023 Analyst Note: Gaining an Edge in VC Investment Selection

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