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Venture Monitor

Q2 2023

In partnership with

Insperity® J.P.Morgan 大成 DENTONS Global Venture Technology

The definitive review of the US venture capital ecosystem

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Executive summary

As the first half of 2023 draws to a close, the venture capital ecosystem is struggling to adapt to a market that has not been seen in years. While the number of factors influencing the market are legion, the benchmark federal funds rate is one of the clearest symbols of change in the market. The current federal funds rate is 5.06%, the highest rate since July 2007, making the low-interest-rate regime that has dominated the financial landscape for the past 16 years roughly the same age as the iPhone.

This shift in the landscape has impacted all sectors and stages of the venture ecosystem with deals, exits, and fundraising all well below the high-water marks set in the past few years. Actors in both the public and private sectors are doing their best to adapt to the realities of a tighter market. On the positive side, technologies such as artificial intelligence promise to provide tremendous value across the economy, and the implementation of bills such as the CHIPS and Science Act offer huge opportunities for the innovation economy. Conversely, a lack of capital and the threat of dogmatic regulation could stifle the development of promising innovation hubs and limit investment activity to existing hot spots.

For investors, the dominant themes of the past quarter have revolved around strengthening their existing positions and making high-confidence investments in new enterprises. In the aftermath of the banking stresses of early 2023, extensive time is going into treasury management. In many cases, local banks that helped administer programs such as the Paycheck Protection Program have become crucial partners for startups that want to make sure they are not too dependent on individual financial institutions. Additionally, startups are cutting costs and pursuing revenue generation wherever possible to increase runway and reduce the need to raise rounds, which are increasingly structured and often flat or down.

With the tightening market, there is an opportunity for the federal government to catalyze both capital formation and technology commercialization across the country. The State Small Business Credit Initiative has allocated $10 billion across the country into funds where venture is playing a significant role. Furthermore, programs such as the Inflation Reduction Act and the CHIPS and Science Act offer considerable incentives for investments in fields such as deep tech and climate tech. If successfully implemented and adopted, these programs will help build the industries necessary for keeping the US economy at the forefront of innovation and providing the jobs to power the economy of tomorrow. Despite these positive actions, some of the regulatory measures proposed by the government also have the potential to stifle capital formation with unintended consequences for emerging managers, especially those investing outside of traditional VC hubs. The Securities and Exchange Commission's proposed regulations around private funds would mandate disclosures of vital strategic information around fundraising and force companies to prematurely go public, causing significant harm to nascent ecosystems in the middle of the country. If implemented, these measures would discourage geographic and demographic diversity in VC, and founders in the middle of the country would be left trying to attract the attention of incumbents based in coastal hot spots.

It would be foolish to attempt to minimize the difficulties of the current market. However, amid these difficulties, there are reasons to remain optimistic. Throughout history, market crunches have often paved the way for the emergence of industry titans. Moreover, specific sectors such as life sciences and artificial intelligence hold countless opportunities within the present market landscape, and there is every reason to expect that the venture industry will continue to be the leading edge of global innovation and the catalyst for building the economy of tomorrow.

NVCA policy highlights

The second quarter of 2023 saw movement on several key NVCA priorities in the legislative and executive branches. The following is a brief overview.

R&D and QSBS tax legislation advances

NVCA sent a support letter for the American Innovation and Jobs Act sponsored by Sens. Maggie Hassan (D-NH) and Todd Young (R-IN). We are hopeful that this bipartisan legislation can pass through a divided Congress.

In June, the House Ways and Means Committee approved the Build It in America Act, which includes a provision that would retroactively restore expensing for R&D expenses (effective for taxable years after December 31, 2021).

The second quarter also saw the passage of the Small Business Investment Act, which modifies qualified small business stock (QSBS) rules in several ways, including a sliding-scale exemption for investments held for three years (50%) to four years (75%); counting the time an investment is held as a convertible note toward the holding period; and allowing LLCs to qualify for QSBS.

NVCA supports both measures. However, work remains to get them signed into law.

CHIPS and Science Act implementation

In June, the Treasury and the IRS issued guidance on the Advanced Manufacturing Investment Credit. This is a refundable 25% credit for the cost of a domestically sited semiconductor manufacturing facility. Startups could utilize the credit or leverage it with other partners in the building or modernization of a facility. There is still time to weigh in on the proposed rules before they are finalized on August 14.

Inflation Reduction Act (IRA) implementation

In June, the Treasury and the IRS released guidance on the direct pay and transferability mechanisms in the IRA. These credit monetization provisions were a priority for NVCA's Climate & Sustainability Working Group and will provide vital liquidity to startups advancing the energy transition.

Additionally, the Environmental Protection Agency (EPA) released details about the $27 billion Greenhouse Gas Reduction Fund (GGRF). The EPA will create three grant competitions to drive GGRF investments into deployment of clean technologies nationally and build local clean-financing capacity.

The EPA also announced new partner connection forms to help applicants to GGRF programs identify partners to incorporate in their applications. Registering through this database could present opportunities for startups to introduce applicants to their technologies and support the decarbonization of the US economy.

Securities and Exchange Commission update

NVCA continues to engage with the SEC Chair Gensler's disruptive agenda:

- Custody rule: NVCA weighed in on a proposal to expand the current rule to cover all assets, including crypto.
- Regulation D ("Reg D"): NVCA continues to watch for a proposal that could force startups to preemptively disclose financing rounds and publish other sensitive business information.
- Recordkeeping enforcement: NVCA joined other industry stakeholders to express concern over the scope of new recordkeeping requirements.

Artificial intelligence takes center stage

AI is having a moment as Washington tries to regulate it while accelerating the pace of innovation. Regulatory and legislative efforts include:

- The Department of Commerce launched a request for comment (RFC) to identify policies supporting the development of trust-building mechanisms like AI audits, assessments, and certifications.
- Senate Majority Leader Chuck Schumer (D-NY) announced an effort to develop legislation on AI regulation.
- Four federal agencies announced a study to examine AI models for fraud and discrimination issues.

In May, NVCA hosted a roundtable with the National Institute of Standards and Technology on the AI landscape. We will continue to keep investors and entrepreneurs at the heart of the AI discussion.

Capital markets reform agenda

NVCA submitted two letters to the House Financial Services Committee outlining the economic impact of VC and supporting the Committee's improvements to the capital formation process. Capital formation priorities passed by the Committee included:

- Modernizing the definition of a VC fund to make acquisitions of secondary shares and fund-of-fund investments qualifying (DEAL Act).
- Increasing the permitted investor and capital limits for 3(c)(1) funds.
- Extending emerging growth company (EGC) eligibility and allowing companies a grace period to transition out of EGC status.

SBA rulemakings

The Small Business Administration (SBA) is working on two issues to improve the ability of government agencies to work with VC-backed startups:

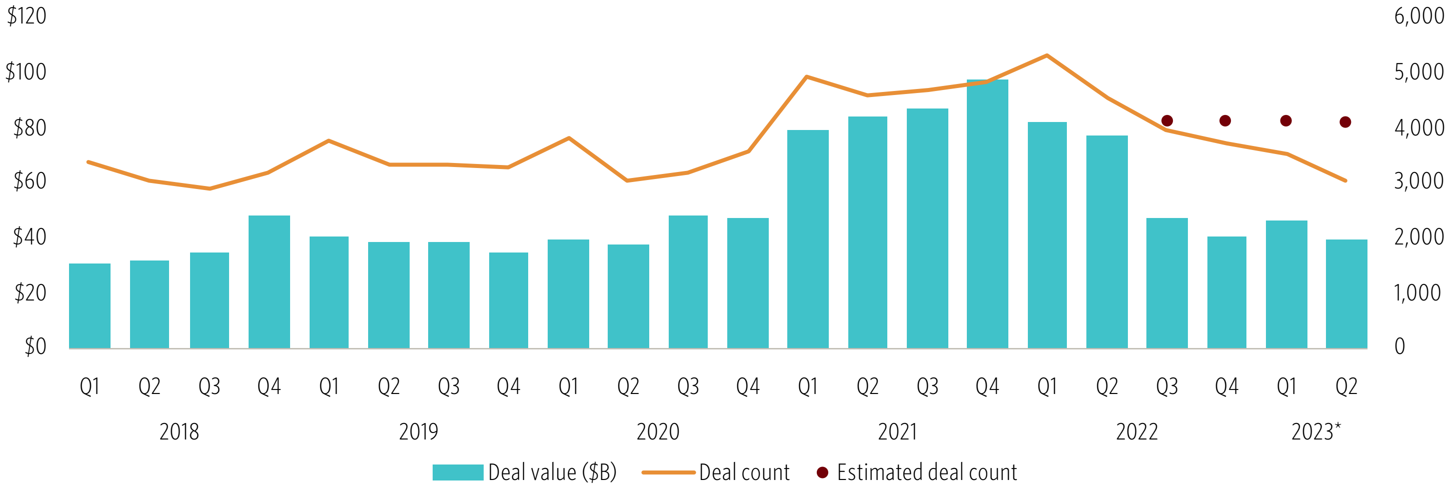
- Affiliation rules: The SBA finalized a proposal to institutionalize the affiliation rules NVCA developed during the Paycheck Protection Program for SBA programs, including the 7(a) guaranteed loan program. We called for the SBA to import the same affiliation rules for purposes of government procurement and the Small Business Innovation Research grant program.
- New Small Business Investment Company (SBIC) accrual debentures license for investors in critical technologies: The SBA is finalizing a proposal to create a new category of SBIC that would allow debt to be paid back after 10 years, when equity investments generally mature. This would allow companies backed by these SBICs to avoid affiliation rule challenges when selling to the Department of Defense and other agencies.

Please see here for a letter we sent to the SBA asking that the new SBIC license category be afforded the same waiver from affiliation rules as existing SBIC licensees.

Overview

Deal count has plateaued

US VC deal activity by quarter



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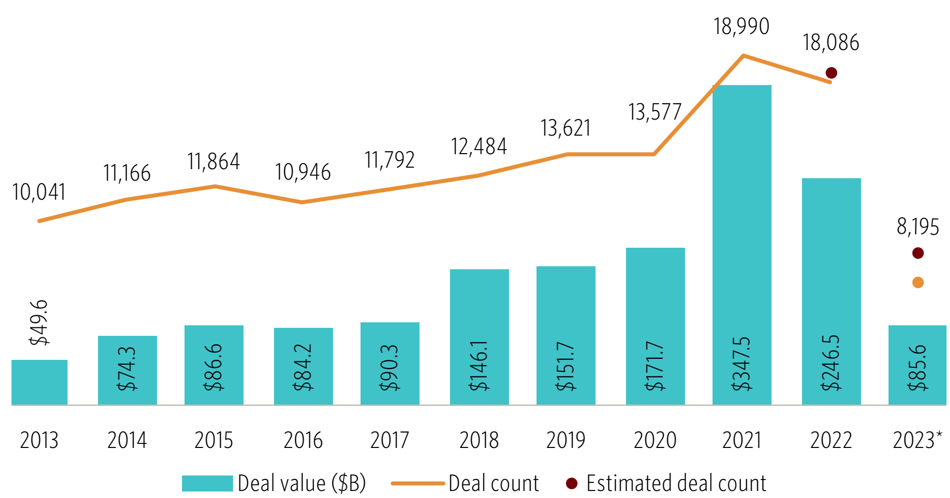
Deal value continues to lag significantly

US VC deal activity



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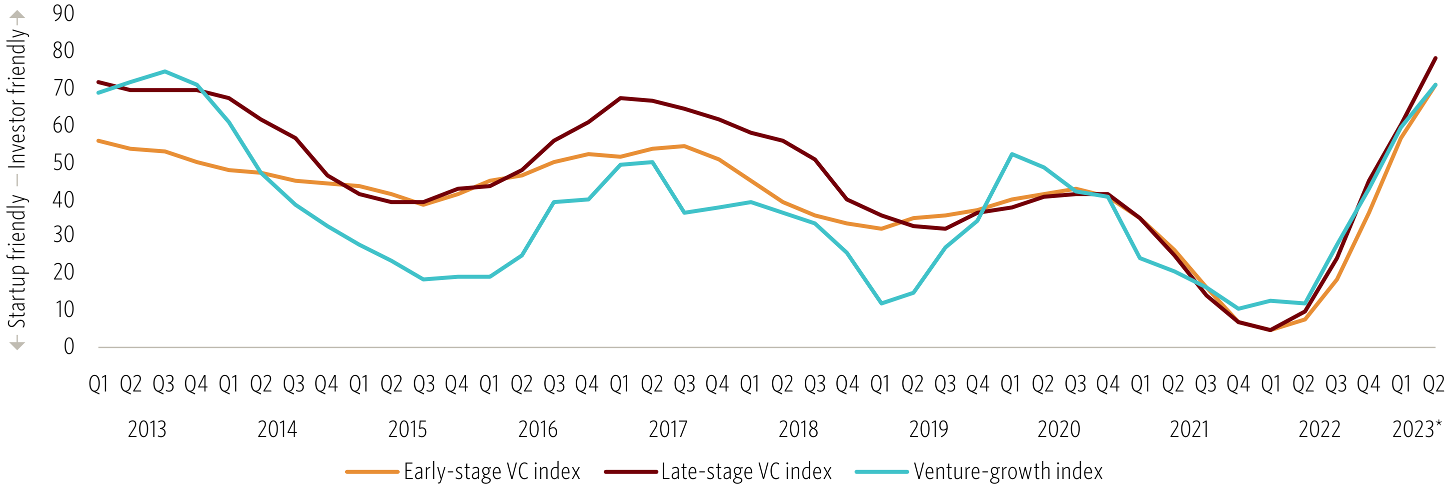
The US venture market operated through Q2 rather mundanely. Deal counts have leveled off, still remaining above pre-2021 figures, and deal value remains low, with few outsized deals to speak of. The tepidness is palpable, and it seems likely the market could quickly hit a cliff if economic conditions worsen. There are now more than 50,000 US-based, VC-backed companies, a figure that has doubled since 2016, and a group that now faces a high capital shortage.

Two stages saw deal count growth in Q2, though for different reasons. The early stage had the fourth-most-active quarter ever in terms of deal count, and there remains a high number of investors looking to this area of the market. Venture growth also saw a deal count increase, but this increase is more likely rescue funding than simply new growth investments. Many companies at this stage should have exited by now, and with the poor outlook, further dilutive capital has been necessary.

Down rounds have finally begun to show in the data. 14.2% of completed financings in Q2 were at a lower valuation than the previous round of the company. Layoffs and debt raised in 2022 surely extended cash runways, pushing down rounds further into the future. We believe it is likely that down rounds will further increase over

Most investor-friendly environment of last decade

US VC Dealmaking Indicator by quarter



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the rest of the year. According to our Dealmaking Indicator, this market is the most investor friendly in a decade, which will pressure valuations and increase dilution for founders. Insider-led rounds came in at the highest in a decade, supporting the idea that more rounds are being completed as extensions or runway top-offs.

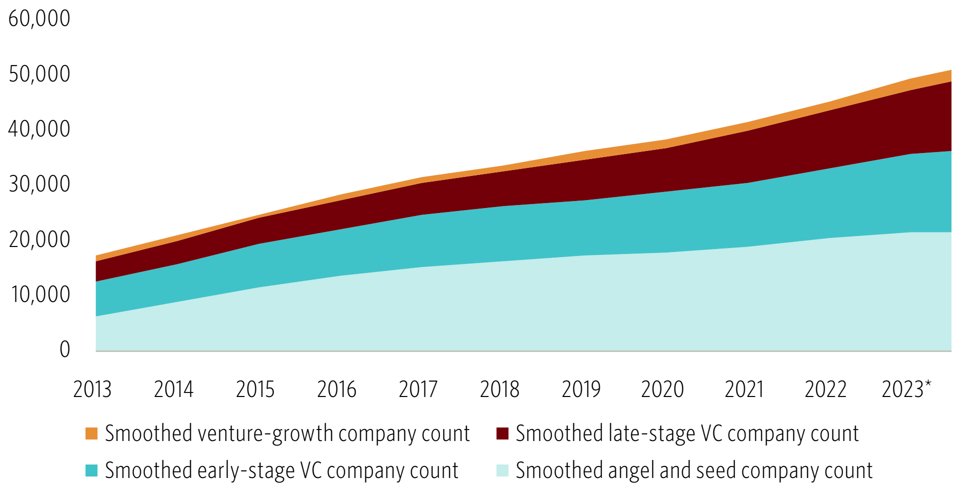
PitchBook's VC-Backed IPO Index and DeSPAC Index have been positive on the year, and the public markets are also showing positive returns YTD. However, there has been little movement on public listings. Public listings generate an enormous amount of exit value, including between 71.5% and 85.1% of the total exit value each year between 2019 and 2021. Now with nearly 700 US-based companies holding unicorn status, a healthy public market exit option is near necessary.

Key takeaways from the report:

- Pressure from scarcer capital availability has trickled down from the venture-growth stage to the earliest part of the venture lifecycle. At the seed stage, quarterly deal value surfaced a 26.3% decline from the previous quarter. A range of factors come into play for this lethargy, including investors devoting more time and resources to existing portfolio companies, deals taking longer to close, and startups resorting to creative capital conservation strategies to avoid coming back to the market.

More than 50,000 US companies now VC-backed

US VC-backed company inventory



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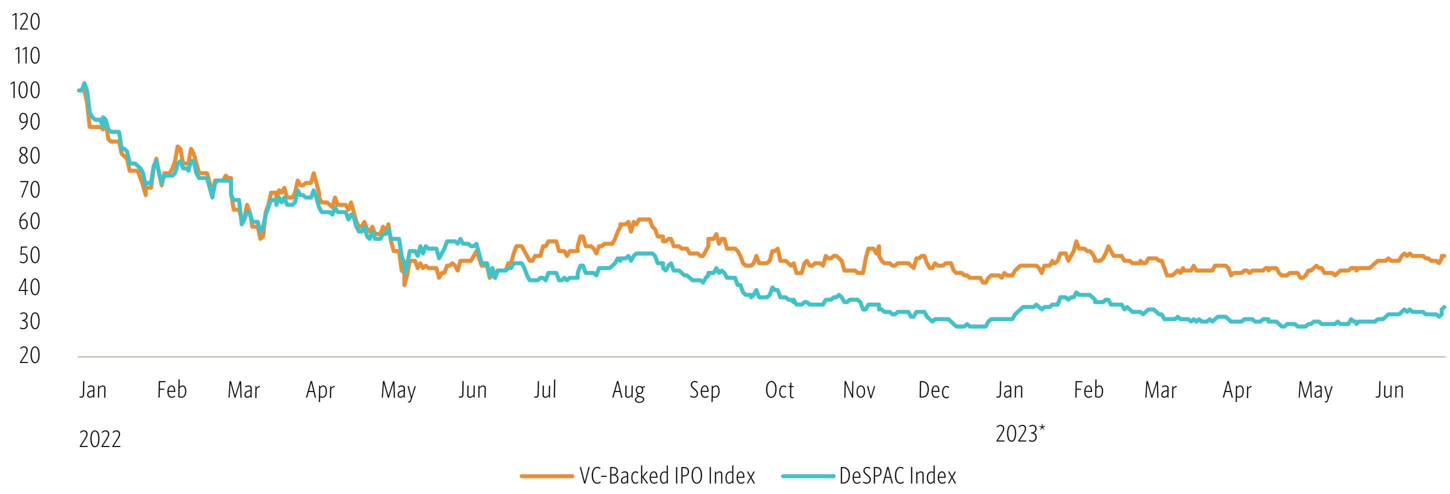
- The significance of nontraditional investors within the venture ecosystem has long been observed, and so has their decreased participation within the VC ecosystem, which continued to decline through Q2 2023. Crossover investors have participated in just under $25 billion of deal value during the first half of the year. That figure is roughly half the record quarterly deal value participation by these investors.

- Through the first half of the year, we observed just $12.0 billion in exit value generated from an estimated 588 exit events. An immense amount of capital remains trapped in late-stage and venture-growth-stage startups hesitant to gamble on whether their financial performance can withstand the intense scrutiny of the public markets. Despite the drab exit activity YTD, Cava's IPO has captured the attention of many, who hope that its success will pioneer a resurgence of the IPO market.

IPO and DeSPAC indexes positive YTD

US VC-Backed IPO Index and DeSPAC Index rebased to 100



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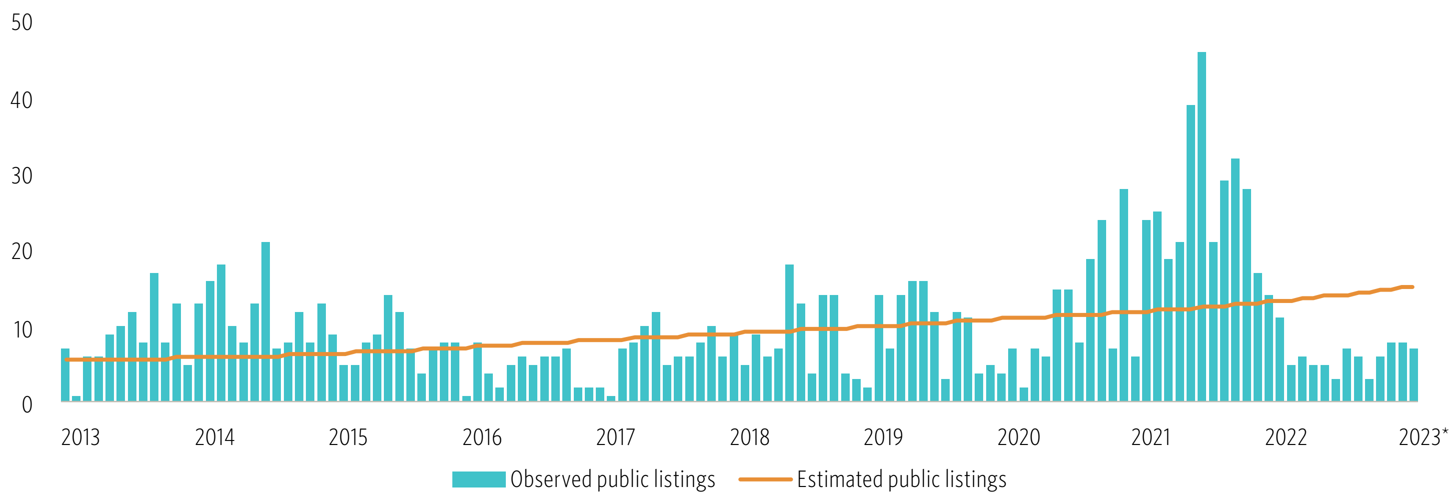
17 months since observed IPOs outpaced estimate

Monthly US VC-backed public listing count versus estimated IPO backlog



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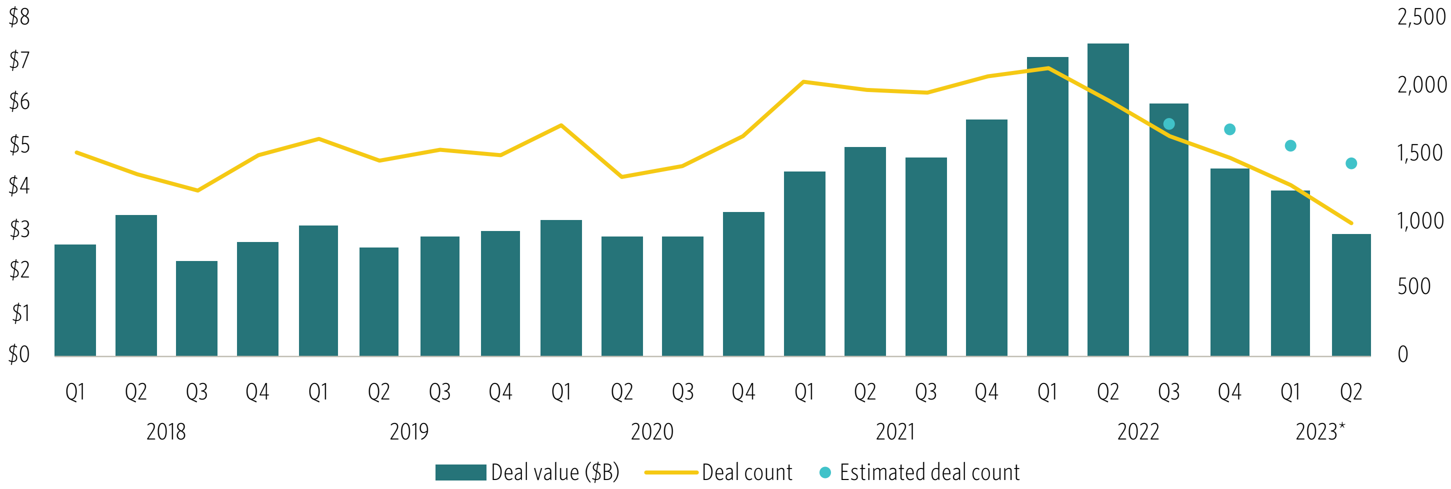
Angel and seed

Q2 angel and seed count experiences a fifth quarter of consecutive decline

US angel and seed deal activity by quarter



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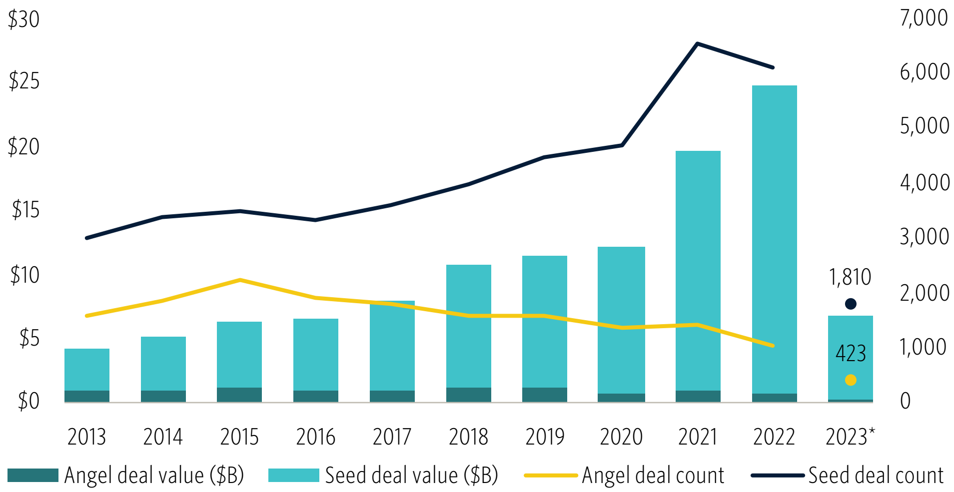
Q2 2023 registered a fourth quarter of consecutive decline in both deal value and deal count at the combined stages of angel and seed. This downward trend illustrates how pressure from dried-up liquidity and a difficult fundraising climate has trickled down to the earliest part of the venture lifecycle. Indeed, nascent stages including angel and seed are insulated from, but not immune to, macroeconomic challenges. The quarterly deal count slipped to an estimated total of 1,451 in Q2, surfacing a 24.7% decline from the same quarter a year ago. For seed, quarterly deal value landed at $2.8 billion in Q2, sliding 27.5% from the previous quarter and representing a significant drop from the dealmaking fervor in 2021 and early 2022. Both a deal value drop and a dealmaking slowdown attest to challenges at the seed stage.

Annualized seed deal value exceeds 2020 figure

US angel and seed deal activity



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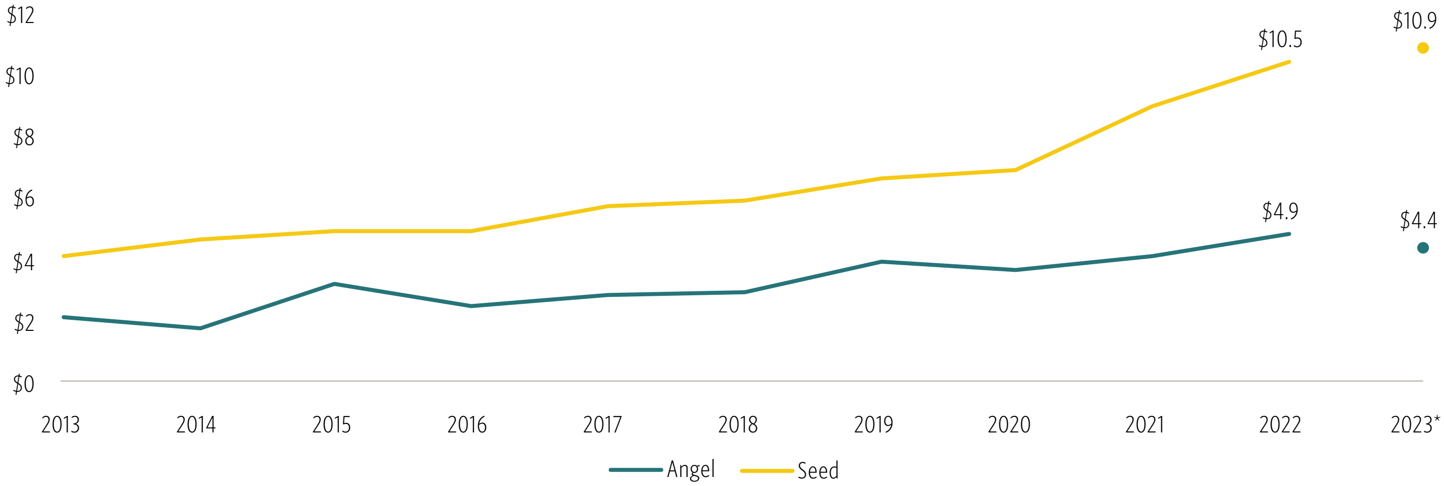
Several factors play into seed-stage lethargy, including startups intentionally delaying raising a next round, investors shifting priorities, and rounds taking longer to close across the board. Many investors have advised their portfolio companies to cut burn and extend runway. Startups have resorted to a range of capital conservation strategies, including reopening the last round and taking bridge financing. In addition, during a market downturn, investors tend to focus on helping existing portfolio companies navigate turbulent waters and reserving capital for making follow-on investments, which leaves them with less time and resources to dive into

Seed valuations continue to expand, while angel valuations contract

Median US angel and seed pre-money valuations ($M)



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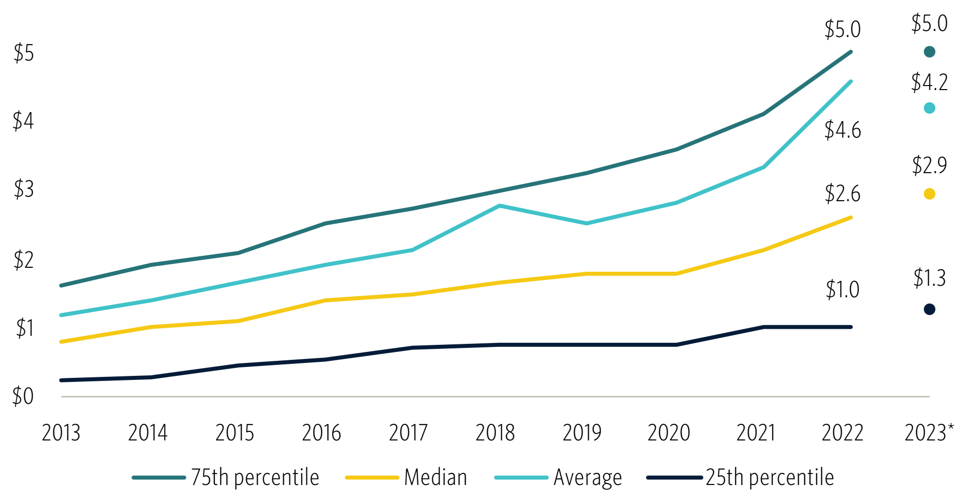
new opportunities. Anecdotally, seed deals are taking significantly longer these days than in 2021 and early 2022, signaling a high level of uncertainty and repricing activity. The dealmaking slowdown at the seed stage primarily resulted from a flight to quality and lengthened process for determining valuation. GPs have now become highly selective when evaluating investment opportunities, taking more time to complete a comprehensive set of due diligence and deal evaluation, whereas previously, when the market was frothy, many had to hasten or curtail this process. The prolonged time window to complete deals also has to do with managers delaying their fundraising process to 2024 in hopes of waiting out a liquidity crunch from the LP lens, stretching their current fund by slowing the pace of capital deployment.

Contrary to market pressures, the median seed deal size continued a YoY growth trajectory, climbing to $2.9 million in 2023 YTD. However, an elevated median deal size enshrouds an increasingly high selection bar for securing seed capital. Anecdotally, seed revenue multiples have fallen sharply, and investors have been advising founders to lower price expectations. What would have been a normal round between 2018 and the beginning of 2022 now seems to be a stretch goal for many founders. While experienced and prudent founders continue to find success gaining traction, it has become increasingly difficult for mediocre businesses to raise what would have been a normal seed round in 2021. While it is still early to identify a trend of lesser-quality companies shutting down, we might see a growing number of those startups failing later this year.

Median seed deal size ascends to highest figure observed since 2013

Range of US seed deal values ($M)



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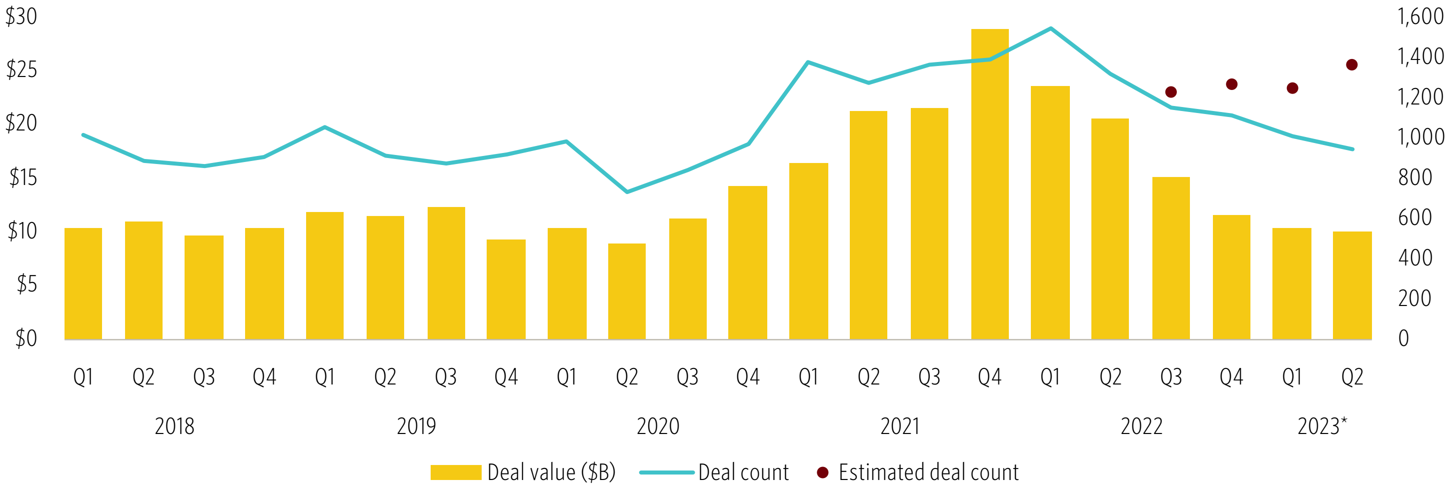
Early-stage VC

Early-stage deal value surfaces a sixth consecutive quarter of decline

US early-stage VC deal activity by quarter



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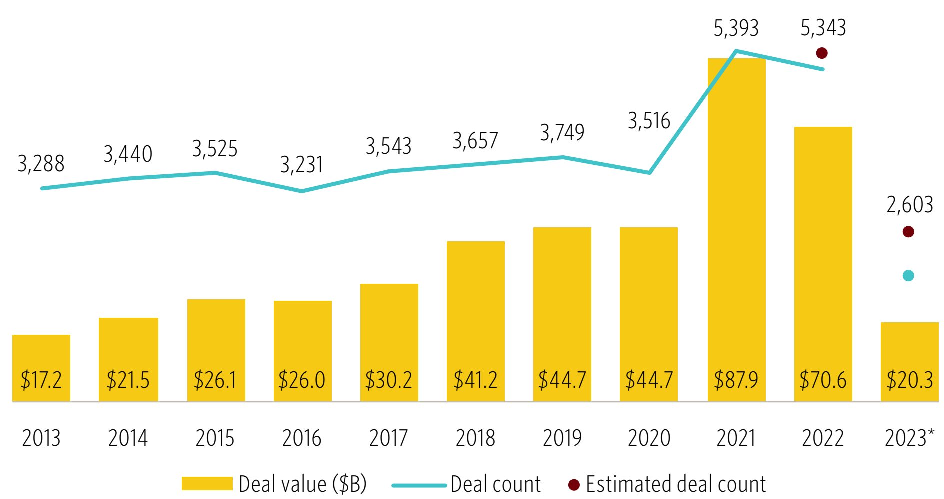
In Q2 2023, early-stage VC displayed a contrarian trend of sluggish deal value and robust deal count. Deal value experienced an eleventh quarter of consecutive decline, settling at $10.0 billion. Meanwhile, the quarter recorded an estimated total of 1,360 deals, an elevated figure that is on par with 2021 levels. Median early-stage VC deal size experienced a second year of steady decline, dropping by 25% from 2022 to $6.0 million in Q2 2023, reverting to the same level as during the onset of the pandemic. In addition, in Q2, 223 early-stage VC deals surpassed the $10 million mark, less than half of the record of 453 from the same quarter one year ago, further attesting the trend of deal size declines.

Annualized, estimated deal count remains robust, while deal value drops sharply

US early-stage VC deal activity



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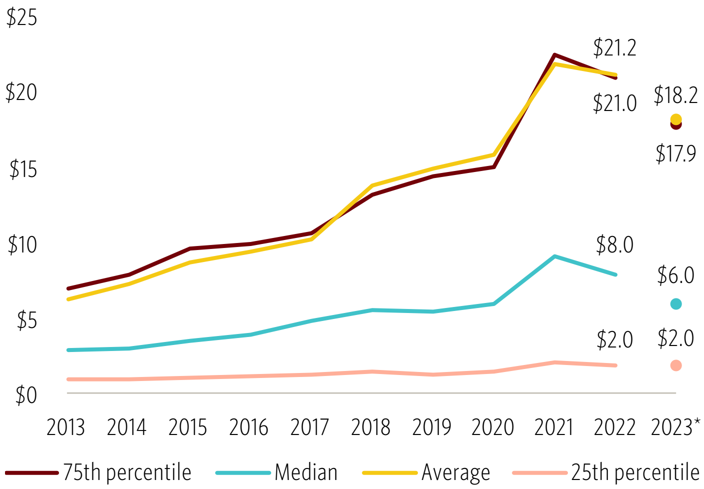
Amid a harsh equity financing environment, the bar for raising an early-stage VC round has gone up across the board. The capital-demand-to-supply ratio for early-stage VC ticked down slightly from the previous quarter, sitting at 1.5x, registering the second-highest level observed in more than a decade. For every $1.50 sought by startups, only $1.00 is supplied from the investor side. To secure equity financing, companies need to show sufficient progress in product development, prove product-market fit, and demonstrate strong traction that it has already received. According to our VC Dealmaking Indicator, as of Q2 2023, the capital-raising environment for early-stage VC startups has turned its

Median deal sizes continue to slip, reverting to 2020-level

Range of US early-stage VC deal values ($M)



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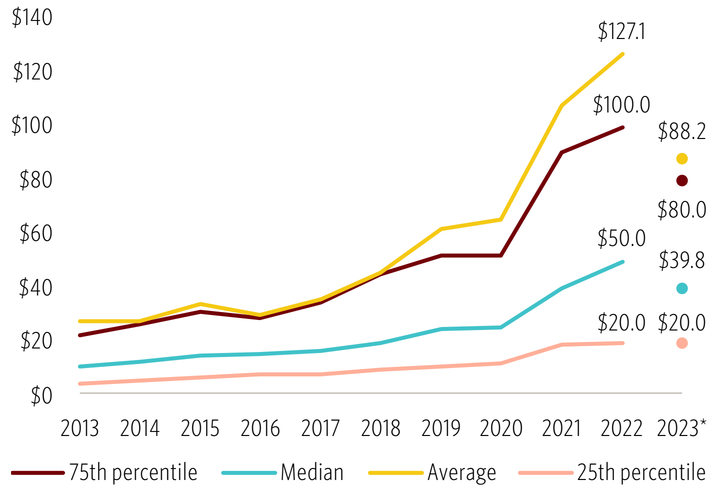
Early-stage valuations narrowly falls below 2021 figure

Range of US early-stage VC pre-money valuations ($M)



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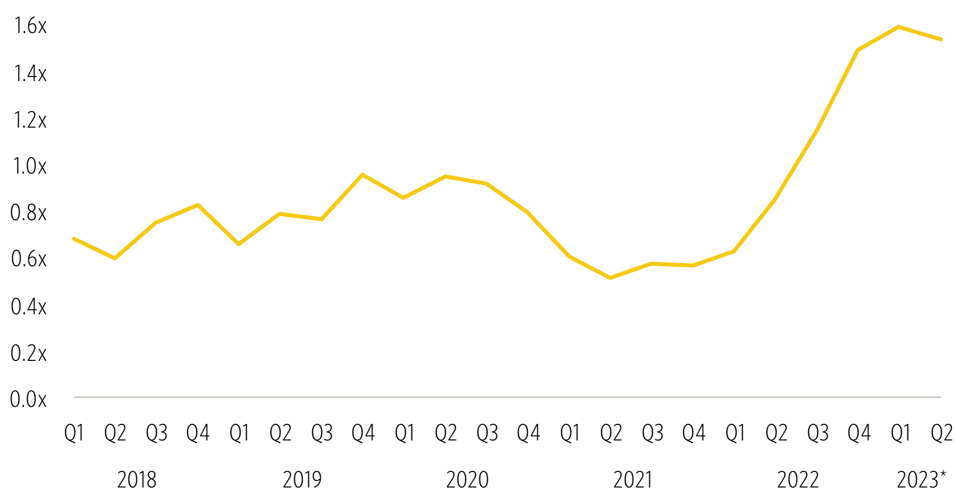
most favorable for investors in 12 years. With dwindling capital availability and more stringent deal terms, investors wield an upper hand at the deal negotiation table. Companies that are unable to demonstrate progress toward the next inflection point via a clear growth path are getting passed on by investors. Against a backdrop of fundraising strain, the days of capital abundance are now in the rearview mirror. Early-stage companies are trying to balance cutting costs with maintaining the ability to steadily progress toward the next milestones. Anecdotally, investors have been advising companies to extend runway for as long as possible while waiting for the financing climate to improve before raising a next round.

GPs have been exercising caution both when examining new opportunities and deploying reserved capital to existing portfolio companies. When making follow-on investment decisions, GPs try to leverage information asymmetry to their advantage while assessing external market signals and evaluating company performance to determine portfolio quality. According to anecdotal sources, during the 2021 capital exuberance, when it was relatively easy for portfolio companies to attract follow-on capital outside of the current syndicate, existing investors often had to make a tough budgetary decision or overextend themselves. With GPs now tightening their reins for capital deployment, investors have started to find helpful signals from monitoring which portfolio companies were able to generate interest from external investors when making follow-on commitments.

Early-stage capital availability falls to lowest point since 2010

Capital demand-supply ratio in the US early-stage VC marketplace



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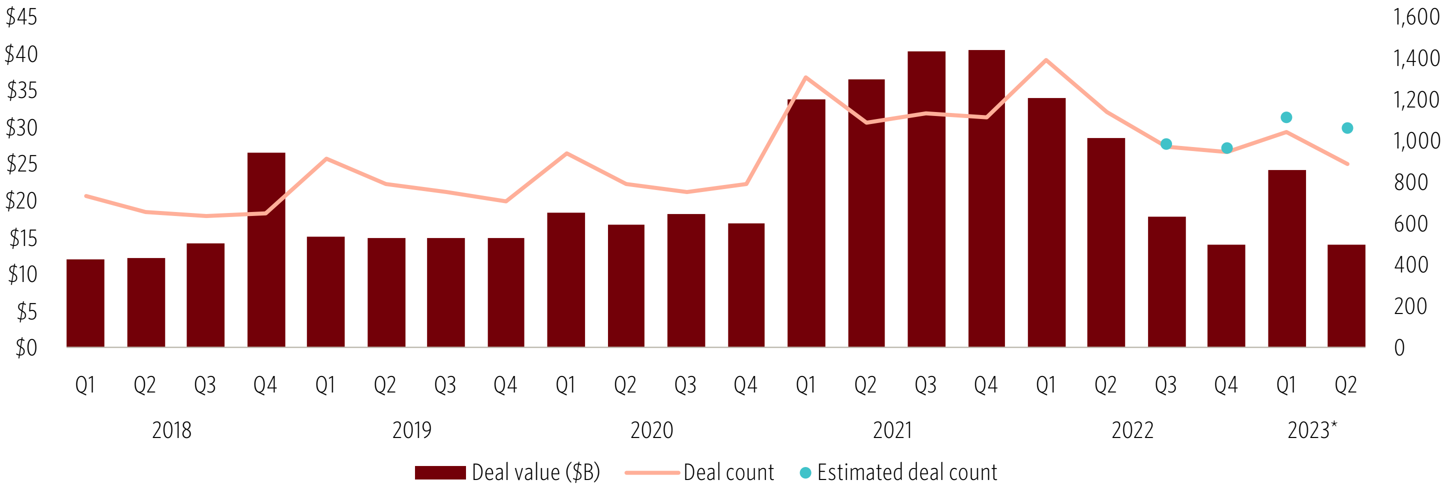
Late-stage VC

Q2 deal value follows broader declining trend

US late-stage VC deal activity by quarter



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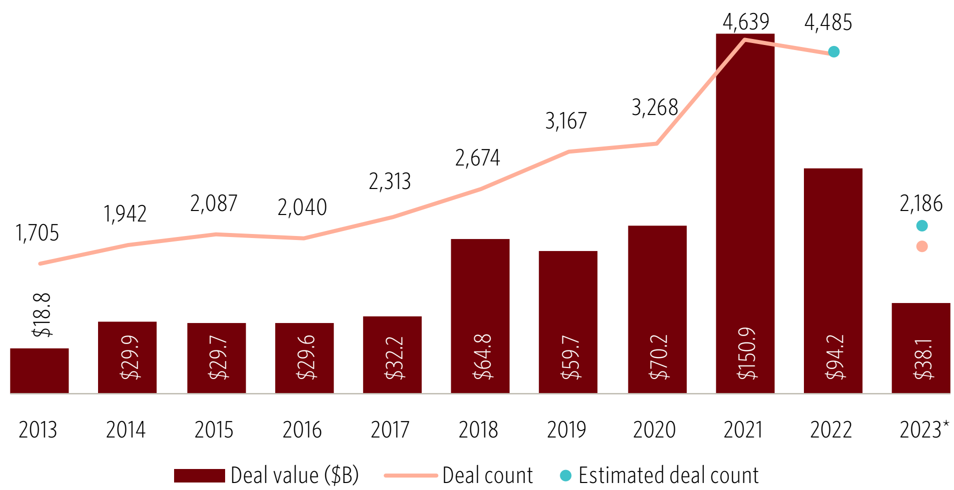
YTD late-stage deal value on pace to set four-year low

US late-stage VC deal activity



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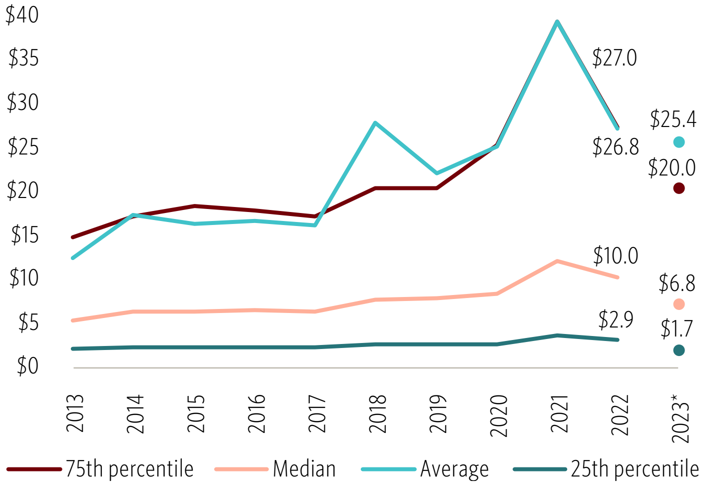
Headwinds continue to challenge the market. The shuttered IPO window and record-high capital demand-supply ratio have continued to pressure late-stage deal activity, resulting in just $13.9 billion in deal value across an estimated 1,071 deals in Q2 2023. Despite market narratives of potential strong returns generated by investing during market downturns, the lack of clarity on whether the VC deal metrics have reached a trough has left a large portion of traditional VC and nontraditional investor capital sidelined. VCs are deploying capital with added caution—investing only in the strongest companies that can weather the storm and have clear paths to high growth. The market has become the most investor-friendly market in a decade, and increasing down rounds highlight this shift.

Sidelined capital, the remaining dry powder in VC funds, and the slowdown of LP commitments to new funds have drastically affected deal metrics at the late stage, with the 2023 YTD median deal size and pre-money valuation landing at $6.8 million and $55.0 million, respectively. This represents declines of 31.7% and 12.4%, respectively, from the 2022 full-year figures. Notably, the median late-stage deal size is nearly on par with the early-stage median, prompting the question as to why startups operating in very different stages of the VC lifecycle are raising similar amounts of capital. In addition to late-stage startups being able to hold off on fundraising due

YTD median and average deal sizes creep closer to early-stage figures

Range of US late-stage VC deal values ($M)



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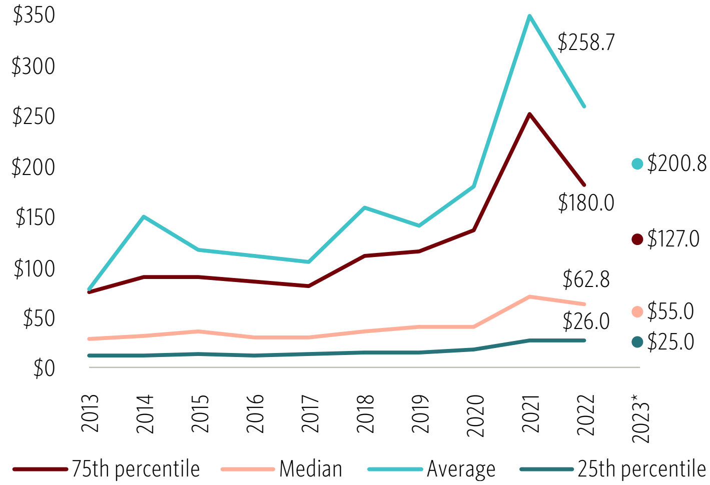
YTD median valuation falls below 2021 full-year figure

Range of US late-stage VC pre-money valuations ($M)



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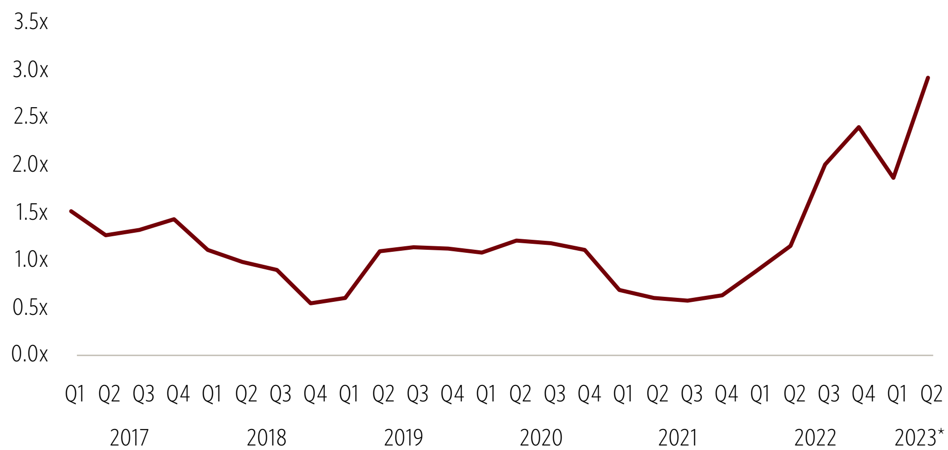
to their overcapitalization in 2021 and early 2022, they likely have more variable costs than their less mature early-stage peers. At a time when capital efficiency is paramount, late-stage startups can make larger cuts to their monthly spending, such as on advertising and marketing. In fact, according to data from Brex, from Q1 2022 to Q1 2023, Series C and D+ startups reduced their spending by 27% and 23%, respectively, more than double that of the spending reduction of early-stage startups.[1] Late-stage startups are raising less capital not only due to investor pullback and a desire to limit equity dilution amid valuation compressions, but also because they can afford to raise less capital.

The large funding gap at the late stage has also meant that fewer outsized deals are being completed. In Q2, just 26 late-stage mega-rounds, or rounds priced above $100 million, were closed. Nearly half Q2's mega-rounds fall into the AI & ML and climate tech verticals, highlighting the interest the market is showing in these sectors. Corporations and VCs alike want to secure access to innovation in these spaces and are clamoring to participate. While late-stage deal activity and metrics have continued their descent, select startups in these verticals will likely elicit the participation of corporations, larger VCs, and nontraditional investors.

Late-stage capital demand nearing 3x available supply

Capital demand-supply ratio in the US late-stage VC marketplace



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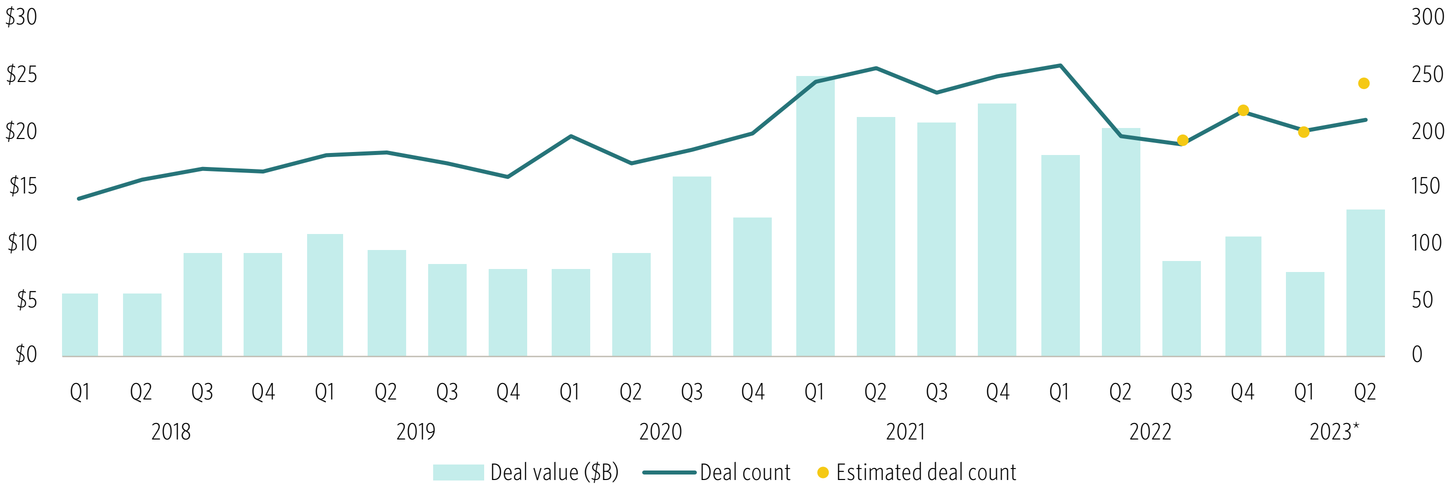
1: "Cost Discipline, Expense Management & Understanding Spend Allocation," Brex, Matt Harney, April 2023.

Venture growth

Venture-growth deal value and count tick up in Q2

US venture-growth deal activity by quarter



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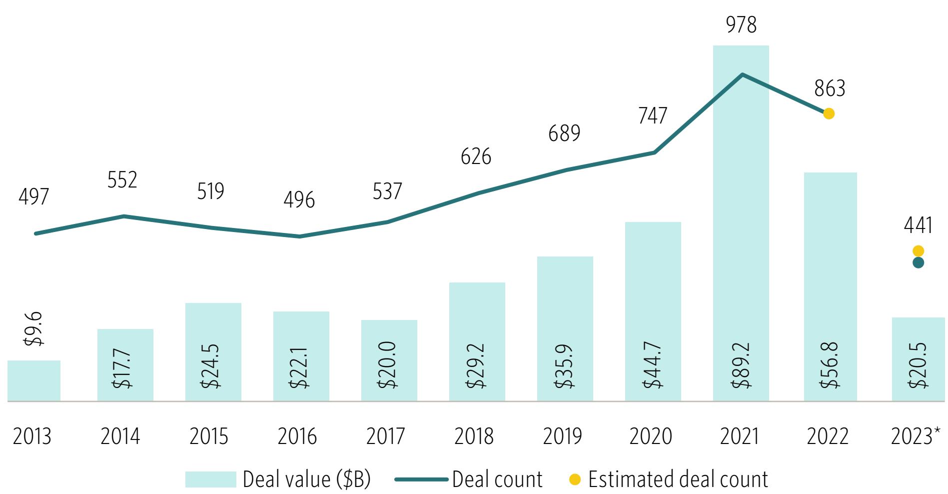
$20.5 billion invested in venture-growth deals through H1 2023

US venture-growth deal activity



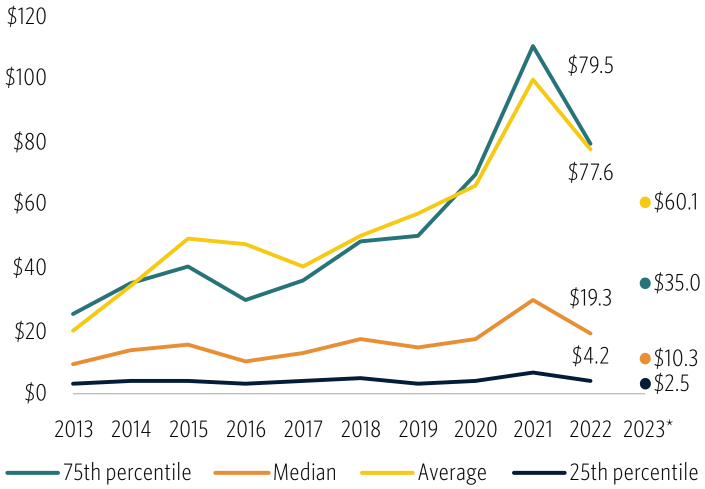
PitchBook-NVCA Venture Monitor
*As of June 30, 2023

Throughout 2023, venture-growth-stage startups have faced significant challenges due to the prevailing macroeconomic conditions. Considering the profound impact that the performance of these startups has on the overall venture ecosystem, the need for these enterprises to strategically adapt is becoming increasingly crucial. Despite accounting for only 7.0% of all closed US venture deals in Q2, this stage recorded $13.0 billion in total deal value, or 32.7% of all the US VC deal for the quarter. It is important to note that Stripe's $6.8 billion Series I deal, initially included in our Q1 report, had its close date amended to Q2. Consequently, we are now including this round in our Q2 data. If we were to exclude the Stripe deal from the $13.0 billion, the quarterly deal value for the venture-growth stage would be around $6.2 billion, accounting for only 15.5% of all US VC deal value generated in the quarter. While this percentage remains consistent with Q1, the absolute deal value of $6.2 billion is approximately $1.3 billion lower than that of Q1. This decrease exists despite the fact that there were an estimated 242 deals in Q2, which is greater than the number of deals completed in Q1.

As of Q2 2023, 200 companies are estimated to be in the IPO backlog. As these companies are unable to go public, many will find themselves operating innovatively in a less-than-friendly exit environment. Different

2023 YTD median deal size falls to nearly half of 2022 figure

Range of US venture-growth deal values ($M)



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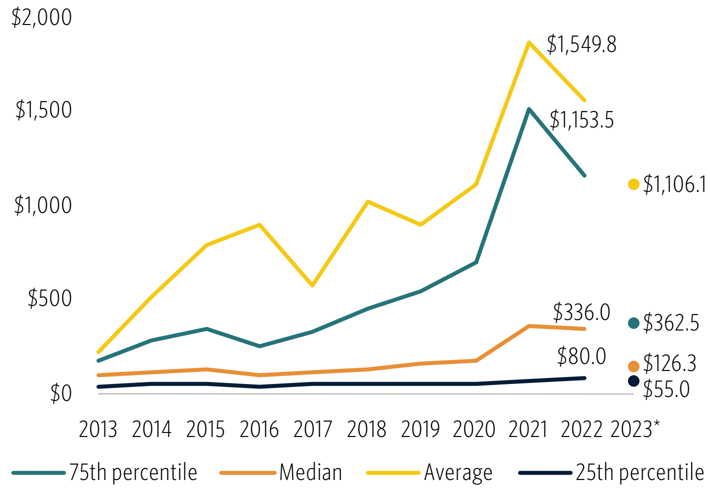
Median pre-money valuation falls to roughly one-third of 2022 figure

Range of US venture-growth pre-money valuations ($M)



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approaches, ranging from raising a down round to even leaving long-term employees vulnerable to tax liabilities, will have pronounced impacts on talent retention and future recruitment efforts. Many companies that raised financing rounds at the height of 2021 have found themselves trapped in a much harsher funding environment when subsequently seeking follow-on rounds, primarily resulting from a pullback of nontraditional investors. There is a limited number of VC managers with sufficient capital to support these cash-burning startups, making companies in the venture-growth stage heavily reliant on large capital infusions from nontraditional investors.

High illiquidity risk, coupled with concerns over valuations, has deterred many nontraditional investors from continuing their involvement with growth-stage deals, leading to a shortage of capital availability. If this trend continues, we anticipate venture-growth-stage annual deal value will fall below the pre-pandemic level of around $40 billion. Our data shows a capital-demand-to-supply ratio of 1.4x as of Q2 2023, meaning growth-stage startups are seeking roughly 40.0% more capital than VCs were providing for new deals. This profound imbalance stands in stark contrast to 2021 and the first half of 2022, when demand-to-supply ratios were below 1.0x, indicating that capital supply flourished and outstripped demand, thereby leading to the imbalance that the market finds itself in today.

Demand-supply ratio declines slightly from Q1 but remains above 1.0x

Capital demand-supply ratio in the US venture-growth marketplace

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A WORD FROM INSPERITY

Three proven ways PEOs keep your portfolio company's momentum going strong

Having time to focus on the vital revenue-generating responsibilities of running a portfolio company (portco) can seem like a never-ending challenge. It's easy to get lost in the day-to-day administrative tasks and lose sight of moneymaking initiatives.

With a professional employer organization (PEO), also known as HR outsourcing, many of your portfolio company's time-consuming HR tasks can be handled by a dedicated team of HR specialists so that you can concentrate on more profitable responsibilities.

Here are three ways a PEO can help you make your portco the best it can be.

1. Help keep you in compliance

With the ever-changing landscape of government regulations and employment law only getting more complicated, it's important to understand how it impacts a portfolio company. Do you know which laws are changing and whether the company is in compliance? Do you know how the Fair Labor Standards Act affects the company? Are employee records in good shape and audit-ready? Are you addressing anti-discrimination and anti-harassment laws?

To avoid this disruption within your portfolio company, you must get ahead of compliance issues. But how do you do this when there are so many other tasks requiring your attention?

That's where a PEO can help.

A PEO can:

- Administer payroll in accordance with federal and state laws and properly report federal, state, and local taxes
- Administer unemployment claims
- Respond to employment verifications
- Comply with many federal laws affecting PEO-sponsored benefits, such as COBRA, HIPAA, and ERISA
- Provide guidance with OSHA
- Assist with healthcare reform compliance

When working with a PEO, you get access to a team of knowledgeable specialists who are well versed in the latest employment and labor laws and regulations that apply to your portfolio company. Their guidance can help make sure that the portco remains in compliance. This can help avoid litigation and fines that can hinder a company's progress and distract from pursuing key initiatives.

"We believe companies should focus on their core competencies. Insperity's core competency is flawlessly delivering the full suite of human resources, payroll, and benefits support to Next Coast Ventures, including a world-class technology platform and a strong managed services team. We recommend Insperity as a valued partner to all of our portfolio companies."
—Jonathan Kaplan Partner, COO & CCO, Next Coast Ventures

2. Develop a strategy for success

Engaged employees help grow a portfolio company and improve your bottom line. You're investing in a company's greatest asset when you focus on creating a positive work environment where employees can thrive.

Likewise, when there is confusion, discord, and lack of direction, a portfolio company can suffer in more ways than you may think. Consider the domino effect this can have on an organization:

- Lost productivity
- High employee turnover
- Lost time and money to recruit and train replacements
- Damaged employee morale
- Dissatisfied clients

A PEO can help organizations cultivate a positive culture, which supports an engaged workforce that is committed to making the portfolio company a success. Engaged employees boost your bottom line, are more productive, and demonstrate commitment. They deliver high-quality customer service and provide a greater return on investment.

Donna Hare
Sr. Business Performance Consultant

Donna JW Hare has more than 24 years' experience in the professional employer organization (PEO) industry. For the past 21 years with Insperity, Donna has been a Sr. Business Performance Consultant advising C-level executives & HR leaders on strategies related to human capital and employment risk with a specialty in mergers and acquisitions, spinoffs, and exit strategies.

Take a look at some of the differences:

Tactical

- Processing payroll
- Filing payroll taxes
- Sponsoring and managing employee benefit plans
- Enforcing workplace policies

Strategic

- Setting employee goals that are tied to business objectives
- Recruiting people who fit the company culture
- Developing motivation and reward programs
- Proactively dealing with conflict resolution

When there is a collaborative work environment that employees appreciate, they'll care more about their jobs and be more invested in the success of the company.

Things to think about:

- What leadership attributes need to be strengthened to maximize the road ahead?
- Is there open communication between the different departments in the company?
- How are things from a financial perspective? Are they where they should be?
- Is there a mission, vision, and values statement that rings true for your company?

It can be hard for HR people to spend time on strategy when they're bogged down with paperwork and administrative duties. Partnering with a PEO gives access to experienced HR specialists who can help develop and implement an HR strategy and lend a helping hand with day-to-day HR duties.

When you are proactively anticipating changes and challenges that a portfolio company may face, your portfolio company is less likely to veer off track when things happen. You save time and resources when you're strategically prepared. The end result is a collaborative relationship that provides a solid foundation for the portfolio company to thrive.

3. Prepare for growth

If growth is the goal, it's important to plan ahead to keep the portfolio company moving in the right direction. A successful growth plan is deliberate and requires forethought.

When you work with a PEO, you have access to specialists who can take a broad look at your portfolio company, employee base, and management structure and advise on how to put the company on the best trajectory for growth.

PEOs take the guesswork out of planning for a company's growth by working to help:

- Identify skill sets the company needs to reach growth objectives
- Create detailed job descriptions and establish a strategic selection process
- Design and implement an ongoing performance management process
- Develop company policies and practices to help limit liability and costly litigation
- Provide guidance on how to establish competitive pay to attract and retain talent
- Develop a company's mission, vision, and values

"Businesses in a PEO arrangement grow 7-9 percent faster, have 10-14 percent lower turnover, and are 50 percent less likely to go out of business."[2]
—National Association of Professional Employer Organizations

Portfolio companies that continue to expand have proven that their strategies, processes, and workforce have what it takes to succeed. But in an unfavorable economy, missteps could be catastrophic. Your growth will be a thoughtful and deliberate process that will continue to support your portfolio company through every growth cycle.

A PEO can help you keep your portfolio company on the right track by taking on much of the cumbersome jobs of HR administration so that you have more time and resources to devote to the portfolio company. When the burdensome responsibilities of employer-related governmental compliance, HR strategy, and growth plans are handled proactively, you have fewer employee relations concerns that can distract from core business objectives—opening the door to success.

At Insperity, we have a long history of helping businesses of any size or sector reach their goals. For more on bringing the benefits of a PEO to your VC firm and your partners, contact Randy Fisher, Insperity's Private Capital Development Director, at randy.fisher@insperity.com.

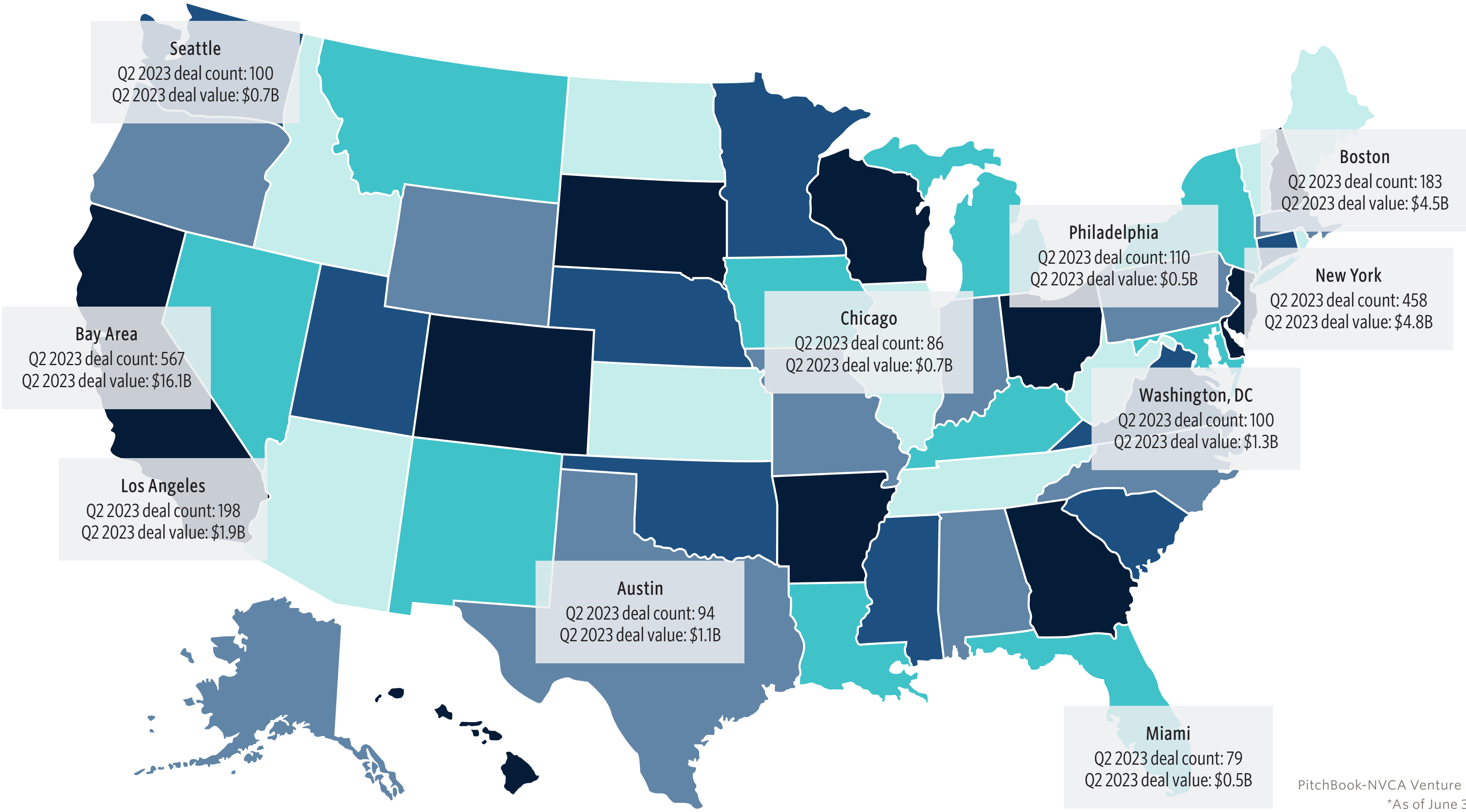
Insperity has helped thousands of startups by providing the HR infrastructure they need to gain the competitive advantage for talent and support their growth. Insperity believes startups are critical to the vitality of the American economy, and we're eager to work alongside up-and-coming companies that share that belief.

2: "PEO Clients: An Analysis," National Association of Professional Employer Organizations, n.d., accessed June 2, 2023.

Regional spotlight

Bay Area below 20% of deal count for fourth consecutive quarter

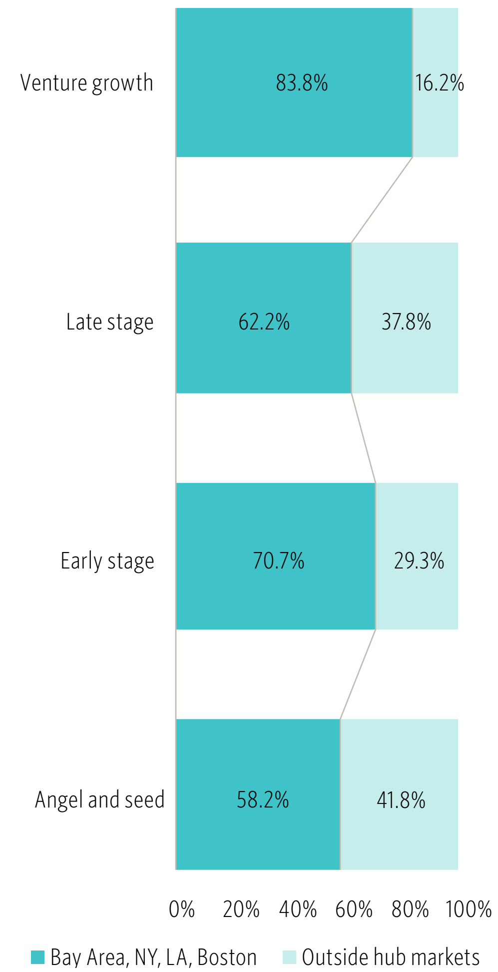
Q2 VC deal activity by ecosystem*



PitchBook-NVCA Venture Monitor
*As of June 30, 2023

Deal value concentrated in hubs

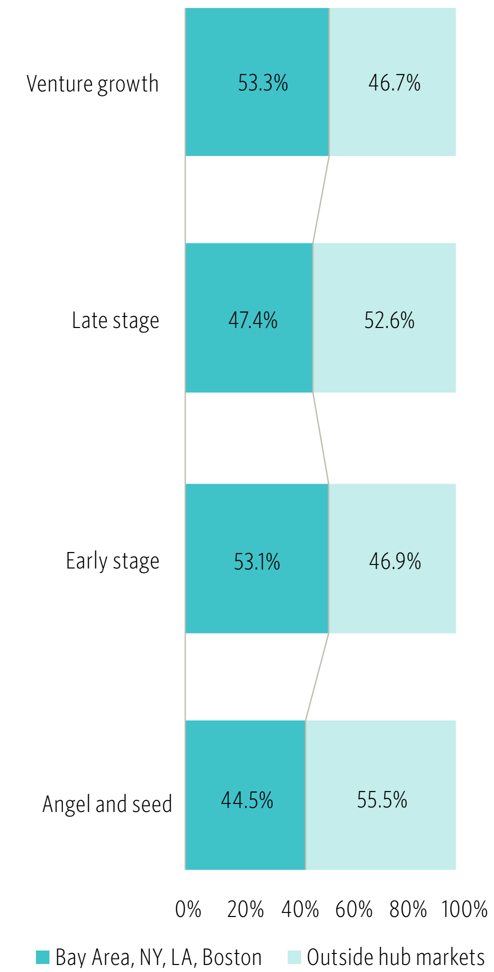
Share of VC deal value by market breakout*



PitchBook-NVCA Venture Monitor
*As of June 30, 2023

Counts more widespread

Share of VC deal count by market breakout*



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*As of June 30, 2023

New York

While its overall deal pace is slower YoY, New York is set to surpass 2,000 deals for the third consecutive year when all is said and done. As the Bay Area loses deal count share, New York's is increasing.

Seattle

Long the fifth-most-active market, Seattle has dropped behind Philadelphia and DC in recent years. Deal value within the ecosystem has also fallen sharply, sitting at just 17.2% of 2022's total.

Washington, DC

After several years of strong fundraising (more than $3 billion raised each of past three years), the DC ecosystem has realized the smallest decline in deal count YoY of the 10 largest markets. The ecosystem should easily surpass 400 deals and challenge to reach parity with the 2022 deal count.

A WORD FROM J.P. MORGAN

Our views on venture

"The resetting of venture valuations is progressing in a relatively orderly fashion thus far. Whether this can continue amid persistent macro and micro headwinds remains to be seen. If liquidity pressures intensify in the coming quarters as we expect, the pace of reset could accelerate."
—Pamela Aldsworth, Head of Venture Capital Coverage

The venture ecosystem is managing through a combination of macro and micro challenges

With short-term interest rates up a sharp 400 to 500 basis points over the past 15 months, there are signs that US economic growth is losing some steam. This is the intended effect by the Federal Reserve Open Market Committee (FOMC), which is tasked with a dual mandate of maximum employment and price stability—for example, inflation averaging 2% over the long term. With the latter well off the mark since mid-2021, tighter monetary policy is meant to slow spending and investment by raising borrowing costs and generally reducing liquidity in the markets and economy. Slower economic activity should cool price-setting expectations over time and bring inflation back down toward its targeted level.

For the startup community, this likely means reduced growth potential in the near to medium term. Until there is greater clarity in the macro outlook, many potential customers are likely to tighten budgets and dial back spending plans. While the US economic expansion has lost some momentum in recent quarters, resilient consumer spending has pushed out the potential onset of recession to later this year or early next. With elevated recession risks on the horizon, business sentiment has turned increasingly cautious, leading to lower corporate IT spending than previously expected and reduced M&A activity. Even the best-performing startups are not immune to the environment, having to revise forecasts lower.

Meanwhile, as the dust continues to settle following the regional banking disruption in March, the outlook for venture lending is emerging as a key area of uncertainty. Silicon Valley Bank was a lender to numerous startups in the venture ecosystem, and the void created by its collapse will take time to fill. We expect moves to diversify deposits and banking relationships by startups and VCs will lead to less venture lending activity over the intermediate term.

Recalibration to the new valuation environment is underway, with a focus on profitability

Over the past 18 months, founders have had to meaningfully shift their focus from a growth-at-all-costs mentality to one of balance between growth, profitability, and durability. This is in response to reduced risk appetite among investors, given the more volatile market backdrop, macroeconomic uncertainty, and slowdown in exit market activity. The Rule of 40 has been increasingly referenced in valuation discussions, with best-in-class companies calibrating profitability to sustainable growth.

Ginger Chambless
Head of Research, Commercial Banking

Ginger Chambless is a Managing Director and Head of Research for JPMorgan Chase Commercial Banking. In this role, she produces curated thought leadership content for commercial banking clients and internal teams. Her content focuses on economic and market insights, industry trends, and the capital markets.

Additional contributors:
Pamela Aldsworth
Head of Venture Capital Coverage
Andy Kelly
Managing Director, Venture Capital Coverage

According to Carly Roddy, Head of West Coast Private Capital Markets, this dynamic has also extended into transaction terms, with a notable shift from founder-friendly to increasingly investor-friendly terms. Structured solutions continue to offer a creative path toward narrowing the gap on valuation expectations. Structured features can include contractual returns, downside protection, and governance rights.

In this environment, fewer companies are announcing valuations with financing rounds, and we estimate up to half of Series A and Series B raises this year have been bridge rounds, predominately insider-led. These bridge rounds serve a dual purpose of holding valuation at the prior round level, while also extending cash runway. Secondary transactions for late-stage companies have also become more prevalent as an avenue to provide liquidity for insiders and employees. These have taken the form of company-organized tender offers or synthetic secondaries, where the company issues a new class of shares and uses the proceeds to buy back equity from insiders.

Effusion around generative artificial intelligence speaks to elemental optimism in venture

Despite the most challenging set of circumstances facing the venture ecosystem in over 20 years, the hype around generative AI in recent months speaks to the optimism and resiliency of the venture mindset. While most segments of venture investing have slowed sharply and valuations are in the process of resetting lower, activity and valuations for generative AI startups remain at all-time high levels. AI's share of venture investment had been steadily rising from 5% in 2012 to over 20% in 2022, but AI has received nearly 50% of all Series B funding year-to-date.

Similarly, seed-stage deals for founders with established track records are active and competitive. As late stages are challenged by prior round valuations and quiet exit markets, more venture investment is funneling toward seed and earlier stages, where investment horizons are longer and commitment sizes smaller.

Some green shoots, but broader reopening of the IPO market unlikely until 2024

According to Alice Takhtajan, TMT US Equity Capital Markets, there have been some encouraging developments in the IPO market in recent months, though a few more pieces need to fall into place to see a broader reopening. Positive signs include a sustained pickup in secondary volumes, lower equity market volatility since late March, and a handful of successful IPOs across the healthcare and consumer sectors.

Other criteria needed to fully open the IPO markets include improved macro clarity with regards to interest rates, inflation, and potential recession. Takhtajan believes this would give investors greater confidence around 2024 and 2025 financial forecasts, and therefore valuations.

Notably, only four tech IPOs have priced in the past 12 months, versus 112 in 2021 at the peak. This is the longest hiatus for tech IPO activity since the 2008 to 2009 global financial crisis, when the window was closed for 14 months.

Normalized markets might see 35 to 40 tech IPOs per year, representing one-third of the overall IPO market.

The good news is that once the IPO market does reopen, the pipeline of companies preparing to go public is quite strong, according to Takhtajan. There are several scaled, profitable, and growing companies that will be well positioned to test the market later this year or early next. This could create a competitive rush for the exits, leaving VCs with portfolio companies that do not get out to have some tough LP conversations.

Given the uncertain and competitive landscape, choosing the right investors is a vital decision for founders

Having investors that can bring value to startups beyond capital is critical in today's environment, according to Luke Sikora, Partner of J.P. Morgan Growth Equity Partners. This group recently closed a $1 billion technology-focused late-stage venture and growth equity fund. Partnering with investors that can provide insights, data capabilities, and access to global networks can be a key differentiator for founders looking to scale and position their businesses for long-term success.

Sikora also believes that young companies benefit from a hands-on approach from investors. Many founders in today's ecosystem lack the perspective of prior downturns and can gain a competitive edge from the experience and expertise investors bring to the table. This is especially impactful when investors come prepared to leverage their own core competencies and networks, adding strategic value to their portfolio companies.

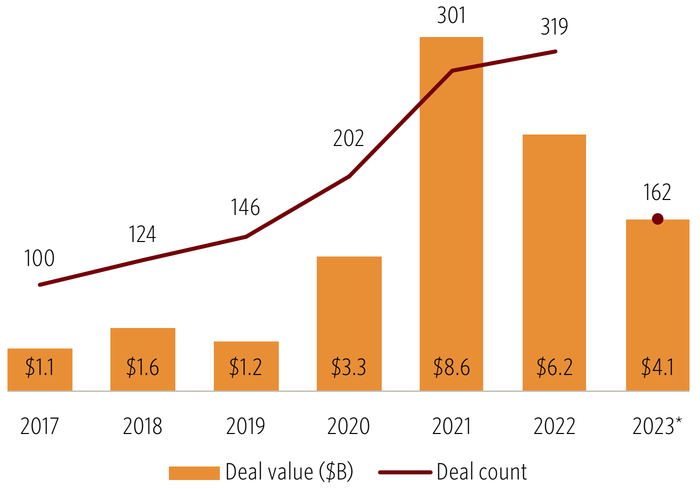
While there has been a retreat of nontraditional venture capitalists since 2021, significant dry powder, coupled with resetting valuations, provides an opportunity for disciplined investors to prudently deploy capital over the next few years.

DEALS BY SECTOR

Carbon & emissions tech

Carbon and emissions tech deal value on track to exceed 2022 value

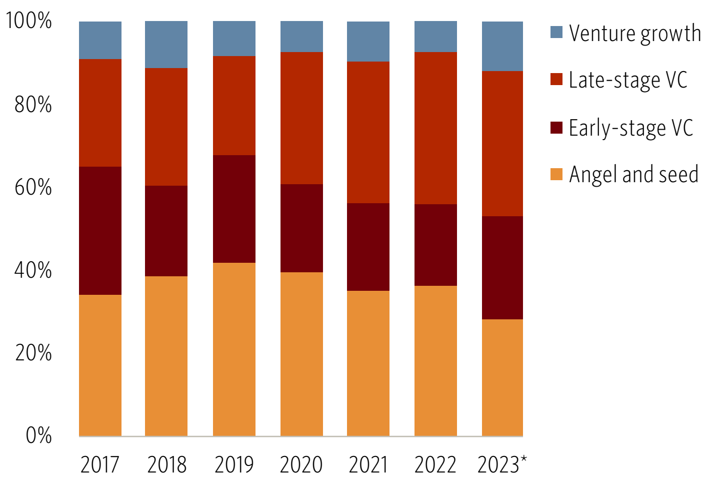
US carbon & emissions tech VC deal activity



PitchBook-NVCA Venture Monitor
*As of June 30, 2023

Early-stage deals increasing in proportion

Share of US carbon & emissions tech VC deal count by stage



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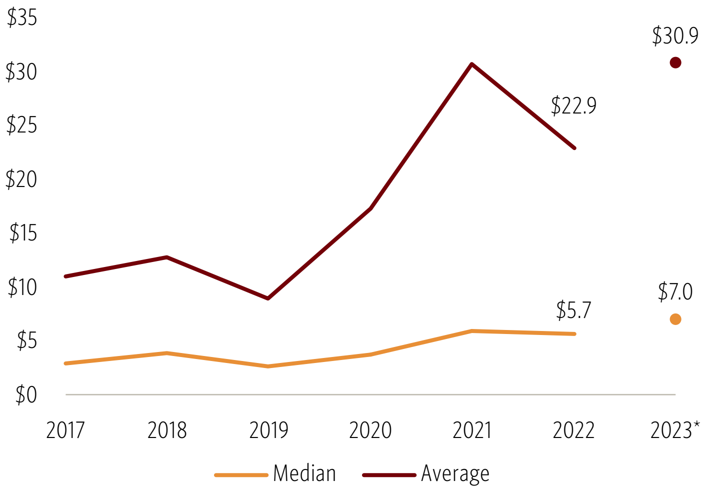
Average deal value returns to 2021 level

Median and average US carbon & emissions tech VC deal values ($M)



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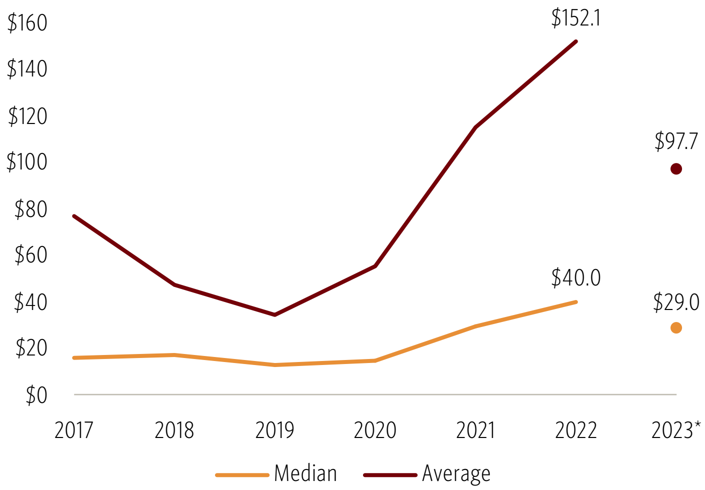
Average valuation falls from 2022 peak

Median and average US carbon & emissions tech VC pre-money valuations ($M)



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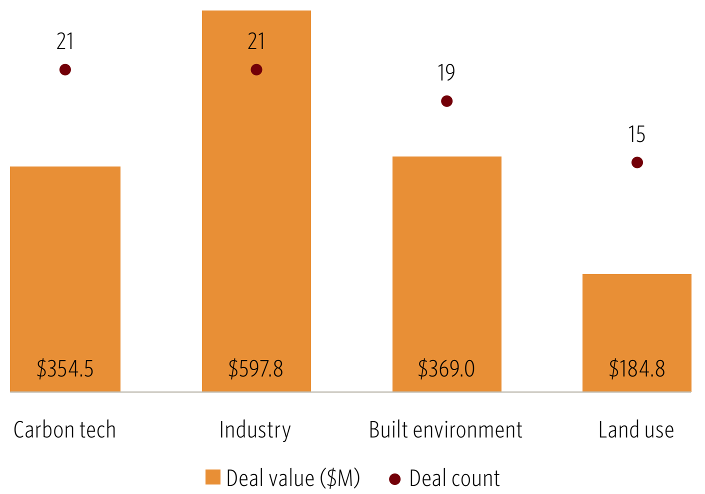
Large recycling deals drive strong deal value for the industry segment

Q2 2023 US carbon & emissions tech VC deal activity by segment*



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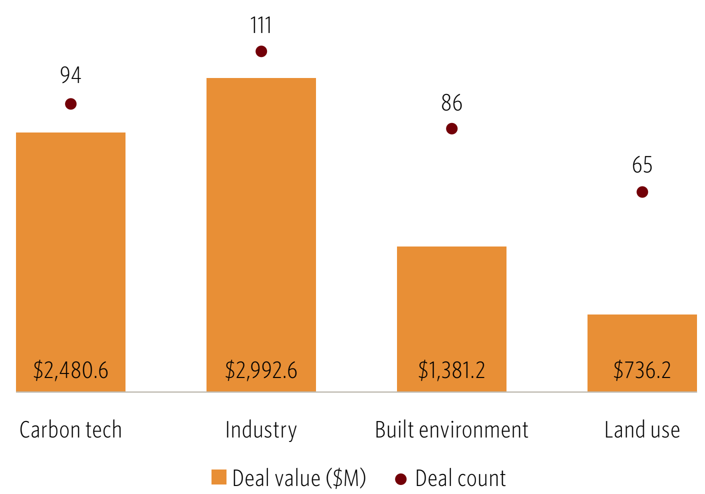
Industry and carbon tech account for majority of funding

Trailing 12-month (TTM) US carbon & emissions tech VC deal activity by segment*



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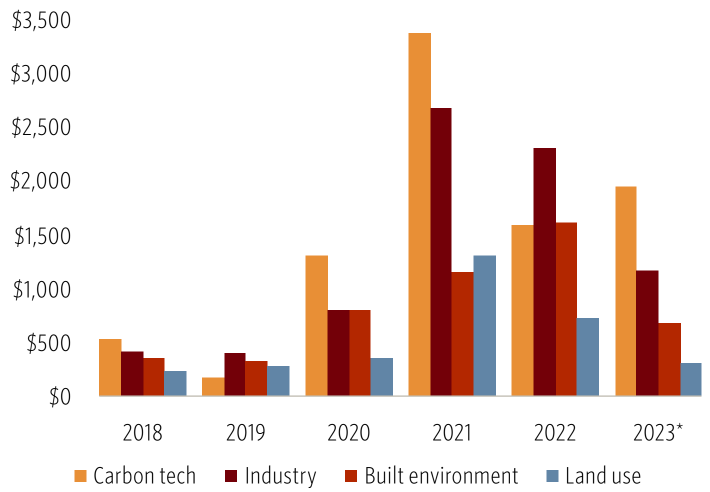
*As of June 30, 2023

Federal support for carbon tech bolsters total deal value

US carbon & emissions tech VC deal value ($M) by segment



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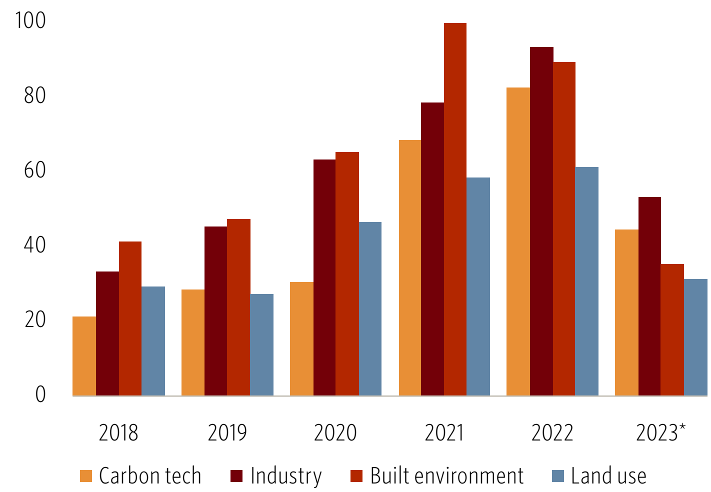
Carbon tech exceeds built environment in deal count in H1 2023

US carbon & emissions tech VC deal count by segment



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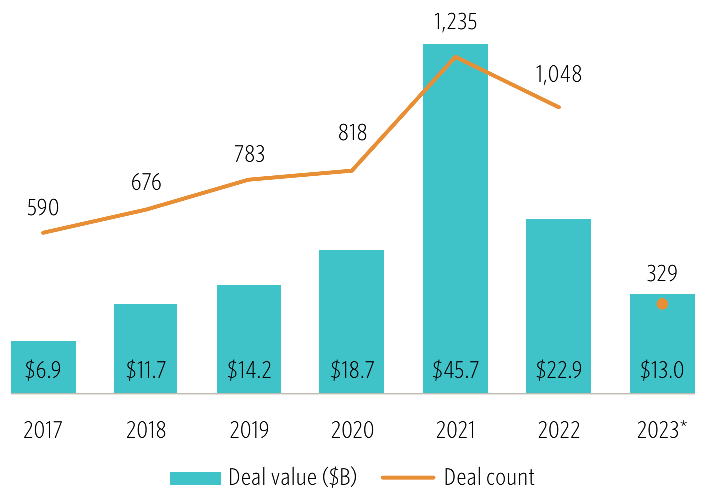
DEALS BY SECTOR

Fintech

US fintech VC deal value on track to surpass pre-2021 levels

US fintech VC deal activity



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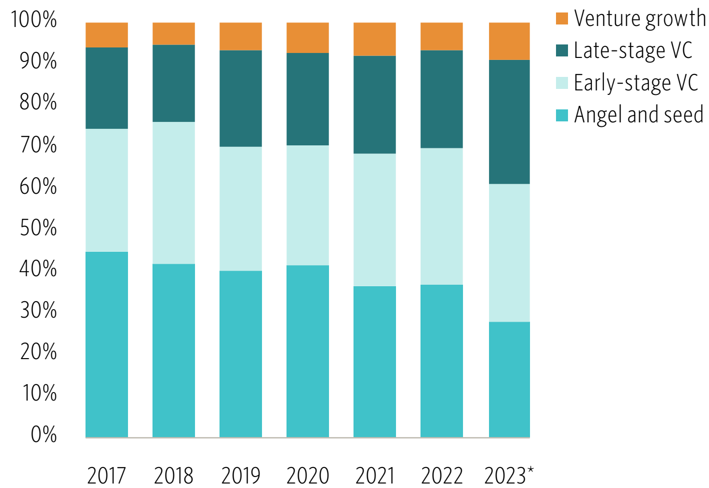
Angel and seed deal counts losing share

Share of US fintech VC deal count by stage



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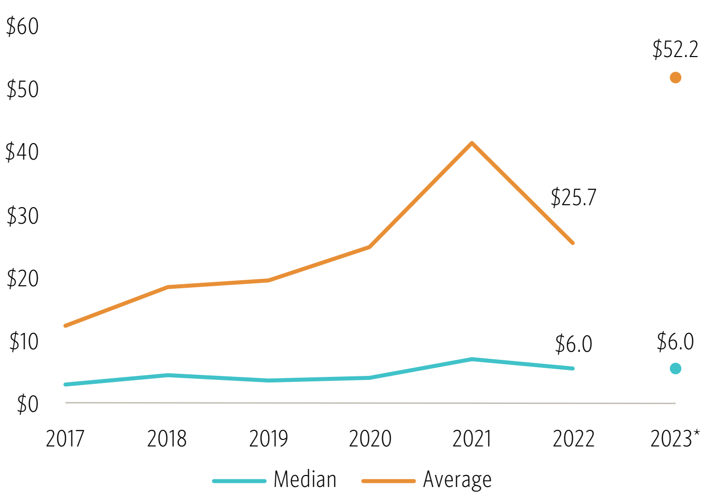
Median deal value remains unchanged

Median and average US fintech VC deal values ($M)



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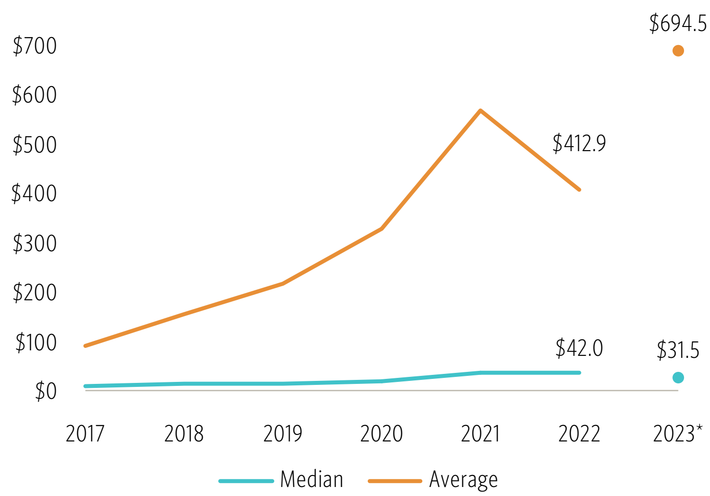
Median pre-money valuations now level-setting

Median and average US fintech VC pre-money valuations ($M)



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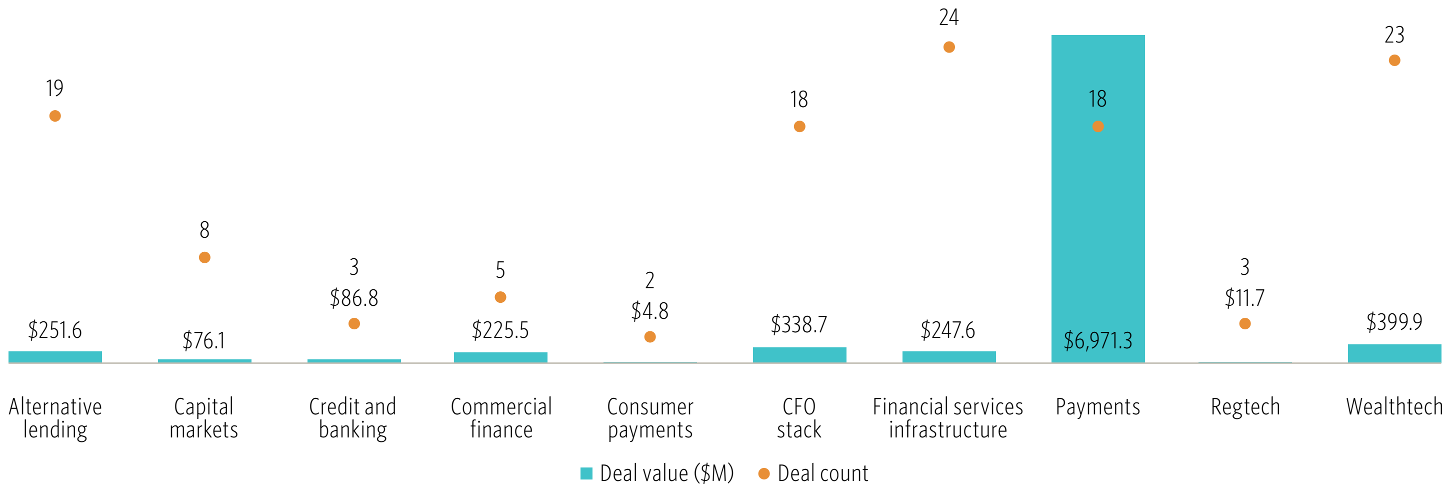
*As of June 30, 2023

Payments lead VC deal activity, driven by Stripe's latest round

Q2 2023 US fintech VC deal activity by segment*



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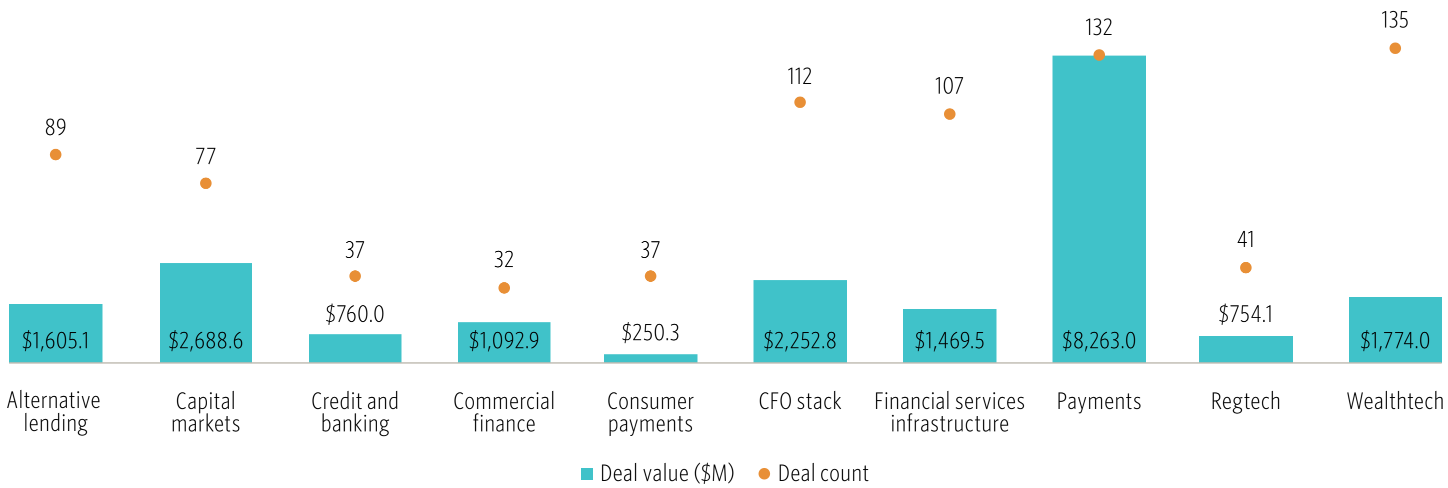
Deals continue to shift toward B2B startups

TTM US fintech VC deal activity by segment*



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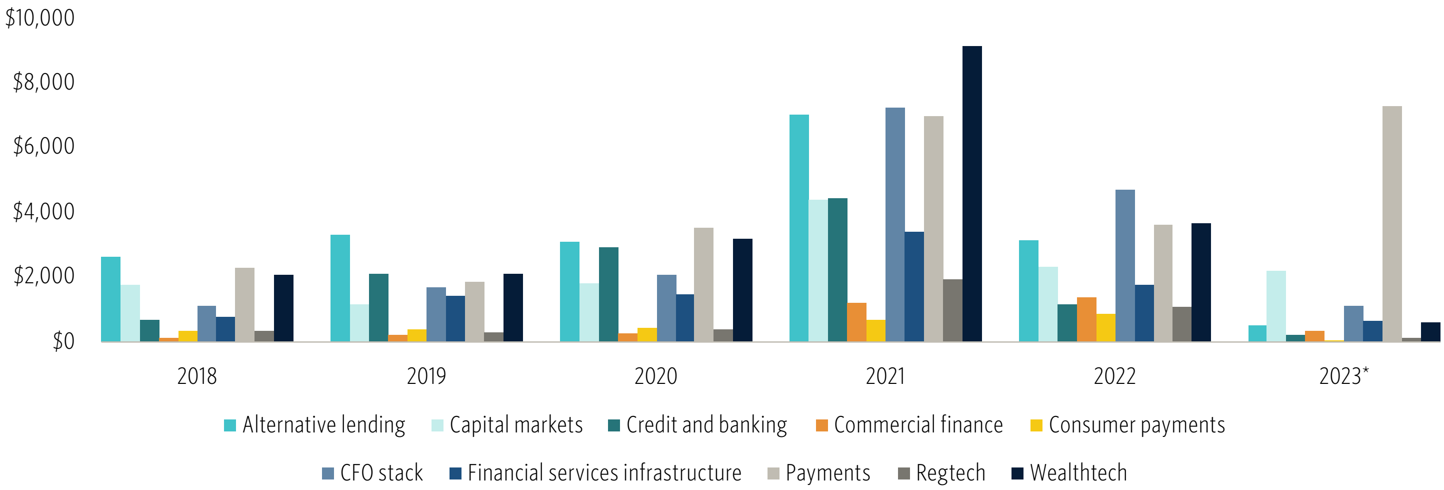
VC deal value decelerates outside of payments and capital market segments

US fintech VC deal value ($M) by segment



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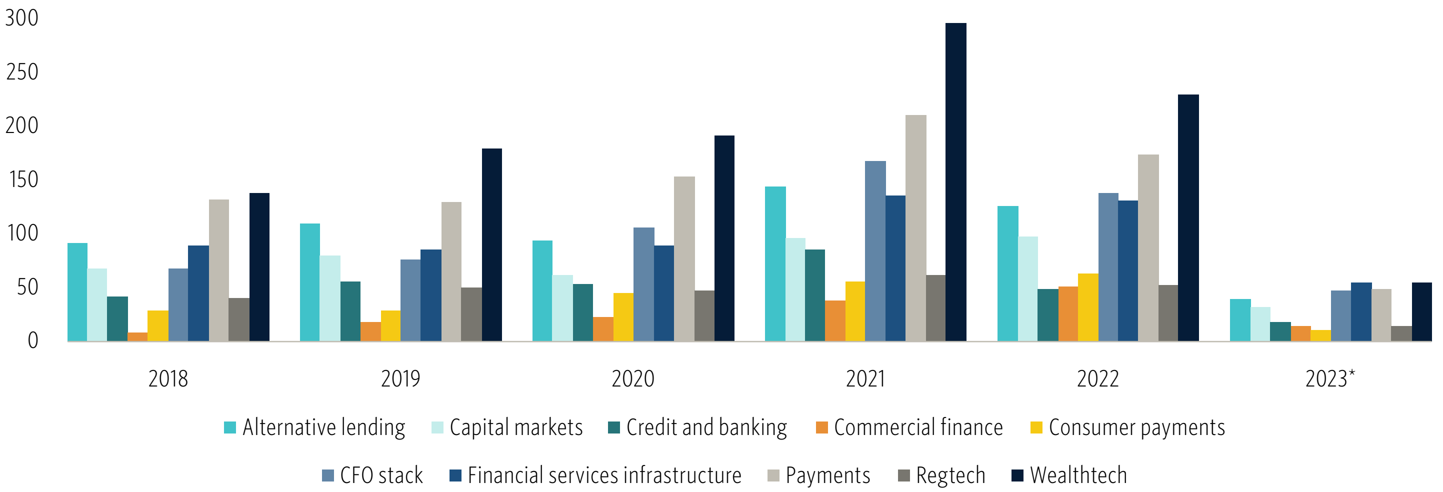
Deal count remains muted in 2023

US fintech VC deal count by segment



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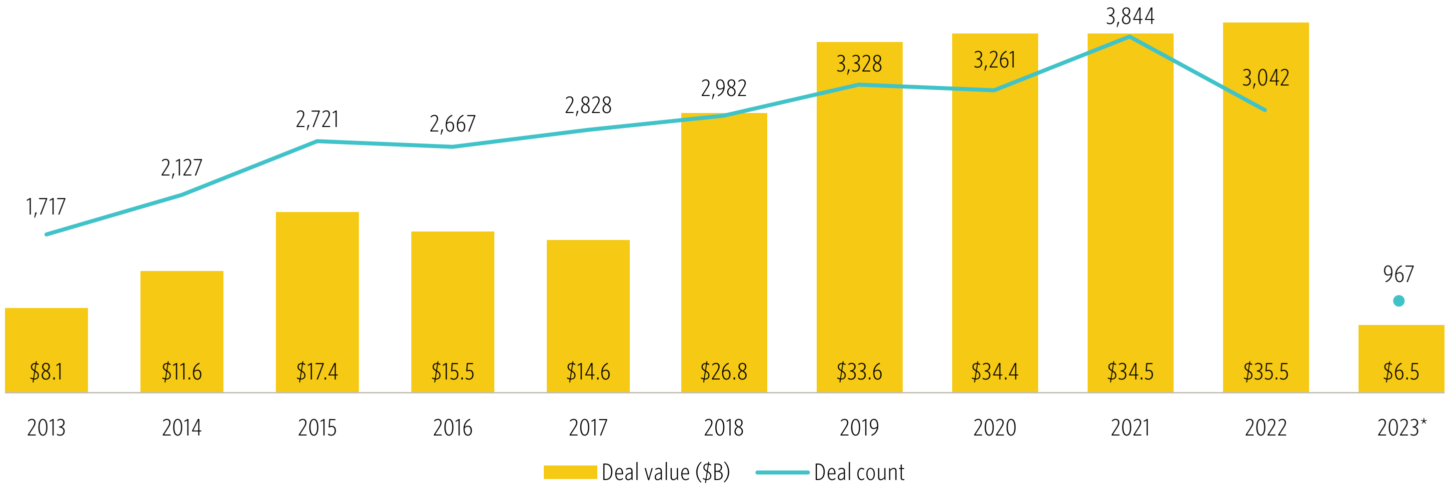
*As of June 30, 2023

Venture debt

Venture debt recovers slightly in Q2

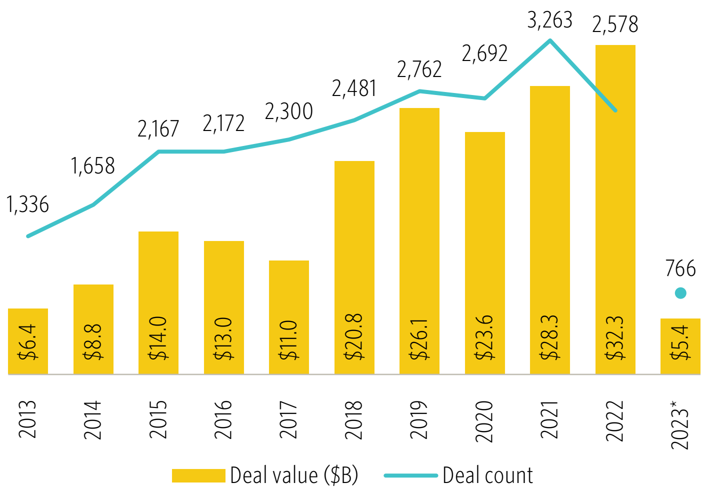
US venture debt activity



PitchBook-NVCA Venture Monitor
*As of June 30, 2023

Tech accounts for 84% of venture debt YTD

US tech venture debt activity



PitchBook-NVCA Venture Monitor
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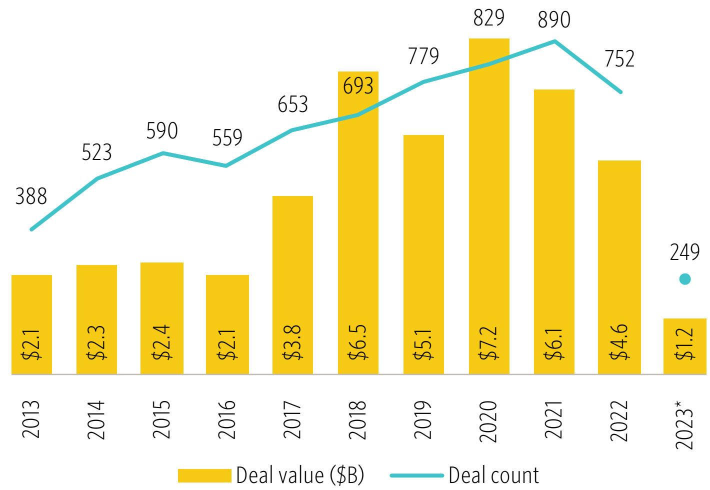
Just $1.2 billion in healthcare debt in 2023

US healthcare venture debt activity



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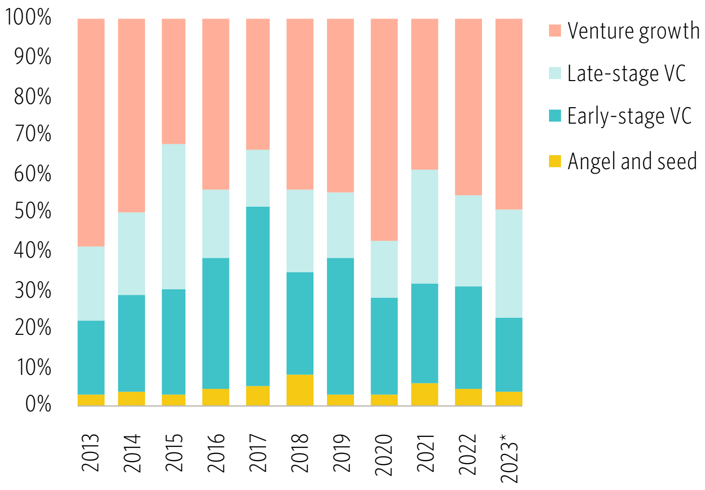
Debt concentrating at later stages

Share of US venture debt deal value by stage



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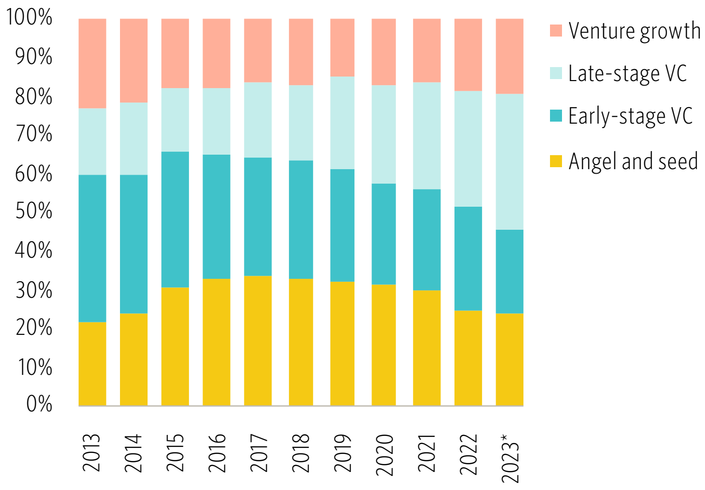
Loans slow across all stages

Share of US venture debt deal count by stage



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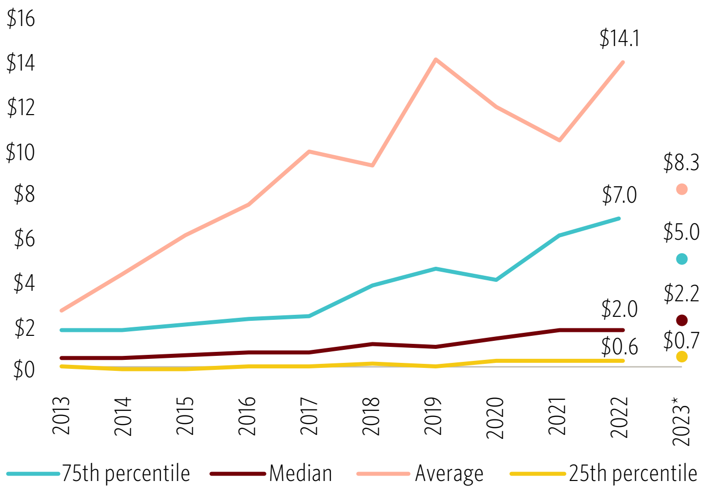
Average loan size lowest since 2014

Range of US early-stage venture debt values ($M)



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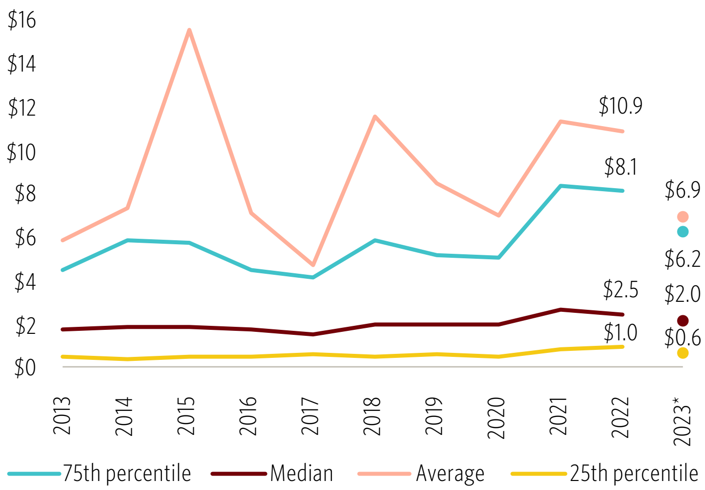
Median late-stage loan size has fallen 22% from 2022 figure

Range of US late-stage venture debt values ($M)



PitchBook-NVCA Venture Monitor
*As of June 30, 2023

A WORD FROM DENTONS GLOBAL VENTURE TECHNOLOGY GROUP

Opportunities and challenges for emerging fund managers

Victor H. Boyajian, Global Chair of Dentons Venture Technology Group, sat down with industry leaders to discuss key opportunities and the latest challenges for emerging fund managers.

Danny Bloomstine *is the Head of Venture Capital, Fund Administration at Juniper Square, an investment management platform based in San Francisco.*

Lorne Brown *is the Managing Director at Encore Equity, a new venture fund based in New York. He is the Former Founder and CEO at Operative Media, an adtech company.*

Bennett Cohen *is the Managing Director at Closed Loop Partners, a venture fund based in New York.*

Henry Elkus *is the Founder and CEO of Helena. Helena Special Investments is an investment unit based in Los Angeles.*

Victor H. Boyajian (San Francisco/ New York): What are you encountering in the market right now and how would you characterize the funding environment?

Danny Bloomstine (San Francisco): I think many investors would agree that you don't want to miss this vintage year. It is likely that the vintages of the last year or two are going to be looked on pretty poorly, so everyone's turning their focus to the current vintage period. The feedback I get from managers is that LPs either feel over-allocated or cautious because they've gotten burned on the last couple of funds. As a result, managers are raising money more slowly and raising smaller funds than they anticipated, which seems to be the new normal. Large institutional LPs are probably holding steady, but for emerging ones, it's definitely a steeper hill to climb.

Bennett Cohen (New York): I think it is important to put money in the market right now and think long term, as this sort of climate is the best time for putting your funds to work. When you're back in market for your next fund, or the fund after that, and then funds seven to 10 years from now, you'll be pointing back to these deals you completed in 2023. When it's easy to raise money, that's likely the worst time to be putting it to work.

Henry Elkus (Los Angeles): LPs are really looking at due diligence processes in this vintage much more closely than they are looking at access, networking, and height. The possible exception is AI startups, which are beginning their own cycle. That is really fascinating to watch, because we're seeing valuations that are unsustainably high in that space right now even though no other space is seeing those. The other thing worth noting is that in this environment, future financing risk is enormous for any early-stage startup.

Chris Errico (New York): What can emerging fund managers utilize or emphasize in their fundraising efforts to really differentiate themselves?

Victor H. Boyajian
Global Chair, Dentons Global Venture Technology and Emerging Growth Companies Group

Boyajian leads a global team focused on representing emerging growth technology companies, venture capital firms, corporate strategics, and private equity firms in a broad array of financings and strategic transactions from Silicon Valley to Boston and New York, and around the globe. The venture team ranks in PitchBook's top 10 for global venture deals.

Chris Errico
Co-Chair, Dentons NY Venture Technology and Emerging Growth Companies Group

Chris is actively engaged in a diverse corporate practice representing investors and fast-growing technology companies across the globe at every stage of their development—particularly those focused on financial services technology, proptech, enterprise software, e-commerce, consumer products, clean tech, digital health, and life sciences.

Christopher J. Kula
Chair, Dentons Funds Group

Christopher focuses on fund formation including structuring, governance, operations and compliance for capital markets, corporate, private equity, real estate finance, and venture technology clients. He has experience working with a variety of private investment funds, including private equity, real estate, and venture capital funds, as well as handling a wide range of corporate and securities work for both emerging and established companies.

Elkus (Los Angeles): Psychologically, a first-time manager without a track record can actually lean into that and the incentives that their situation creates. Oftentimes, the partners at larger firms won't have the connections to king-make, so it's going to be a junior partner in the deal that has the right incentive structure. We simply cannot fail. And so, we will invest the time and resources to ensure we don't fail. Operationally, if you can show that you've brought in customers, it's a way to actually show a track record without an economic result.

Lorne Brown (New York): In this environment, you have to show the market something different, whether it's an LP or a CEO that stands out. We like to think about business model 4.0, where you're really lining up the value so that it leans toward the customer. I also always tell CEOs that we're going to evaluate not only their market and their product, but also if they can be coachable.

Christopher J. Kula (New York): What are the qualities that characterize a successful team at an emerging manager?

Brown (New York): It's crucial to recognize your own strengths and weaknesses. What skills and personalities do you need to complement you? Build a team around you that can answer those questions.

Elkus (Los Angeles): When you are too small to have everything that you want, you have to ask: What do you really need, and what are you willing to set aside? What does my firm purport to do that is unique? And how can I hire specifically for that? How can you be the best in the world at that one function and prove that to my LPs? After that, you can scale and fill in around the core you began from. A mistake people make is to hire people who don't address that core need. Maybe they want to have an impressive "Our Team" page on their website to show to funds—but those hires turn out to be too expensive as a percentage of their available fee and carry. On the other hand, if you first bring on folks you know and trust, and who have the network to help you, you have the dual benefit of setting the right culture and avoiding ego clashes early on.

Kula (New York): How do you allocate time among fundraising, dealmaking, and sourcing?

Cohen (New York): In the early part of the initiative, when you're putting your story together and getting those first closes done, it's much heavier on the fundraising and LP networking side. Then, hopefully, it sort of shifts and you get into the flow with your fund. Then you get a little bit of a break, allowing you to be more focused on the market and investing before you go out for the next fund. The danger is, if you spend all your time fundraising in those early cycles, you may lose track of what's happening in the market.

Elkus (Los Angeles): Ideally, you have conversations with LPs that also benefit your portfolio companies and your understanding of the market. That way it's not a zero-sum game. If you can call LPs that own the companies that could be customers for your portfolio companies or your current prospects, and find those synergies, then you can construct a system where you're spending your time efficiently every day while also meeting your fiduciary duty to your investors.

Boyajian (San Francisco/New York): Are you bringing your CEO LPs into your early fundraising meetings to attract other LPs or CEOs?

Brown (New York): Yes, it is something I do lot. It is a great way to get immediate feedback, leverage their expertise, and to keep LPs engaged.

Errico (New York): What is one piece of advice you would give to a younger version of yourself operating in this kind of environment?

Cohen (New York): Continue to put money into the market, even if it's smaller amounts or it's outside the fund structure that you're currently working on. Know your track record and build it. Consistency helps build your momentum and your credibility when you're fundraising.

Brown (New York): In all seriousness, get a life coach. These are hard jobs that we're all doing, and when you're managing multiple parties and a lot of money, the stakes are high. It can be confusing. You can kind of lose yourself a little bit. You can get over-indexed on outcomes and desires a lot of times. When that happens, take care to recenter yourself. Spend time on your own mental wellness.

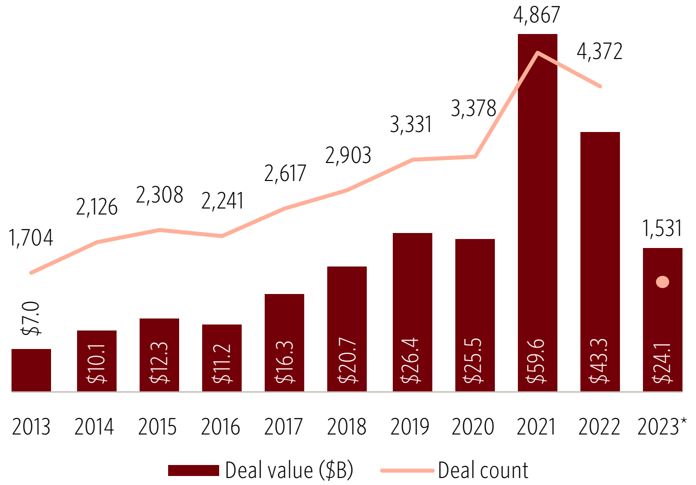
Bloomstine (San Francisco): If you want to be an investment manager, rely on your advisors to help you along. Don't try to recreate the strategy of the industry when you're starting out. Find your lane, and when you find success in that, then you can start to get more creative.

Elkus (Los Angeles): First, when you're in conversation with a potential investment, put the time in to respect their field by really learning and reading about it, as opposed to parachuting in and learning on the spot. Second, remove as many buzzwords from your vocabulary as possible. Communicate clearly and concisely. It demonstrates that you actually understand the subject.

Female founders

2023 pacing for second-highest total invested in female founders

US VC deal activity for companies with at least one female founder



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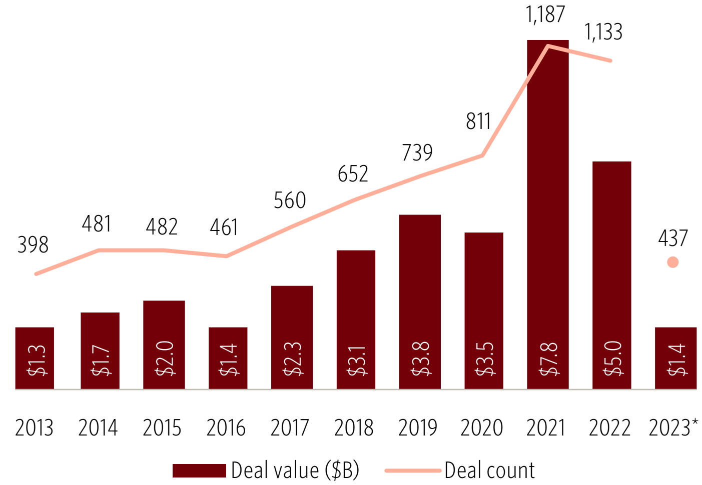
All-female-founded companies struggle to raise in 2023

US VC deal activity for companies with all-female founding teams



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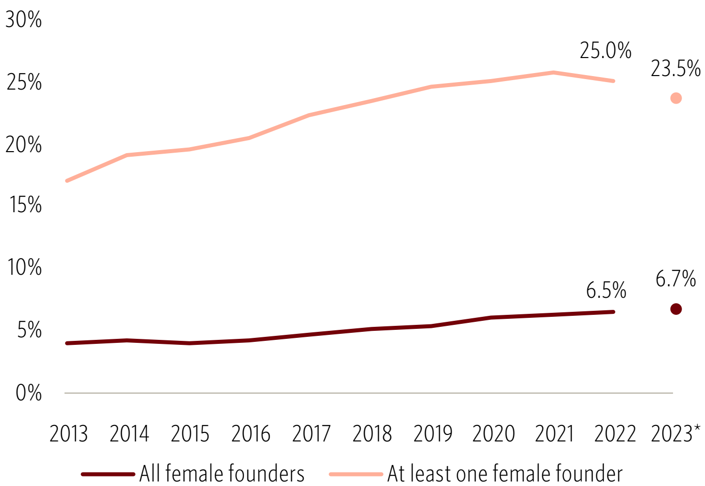
All-female-founded companies increase their proportion of total deal count

Female-founded company deal count as a share of all US VC deal count



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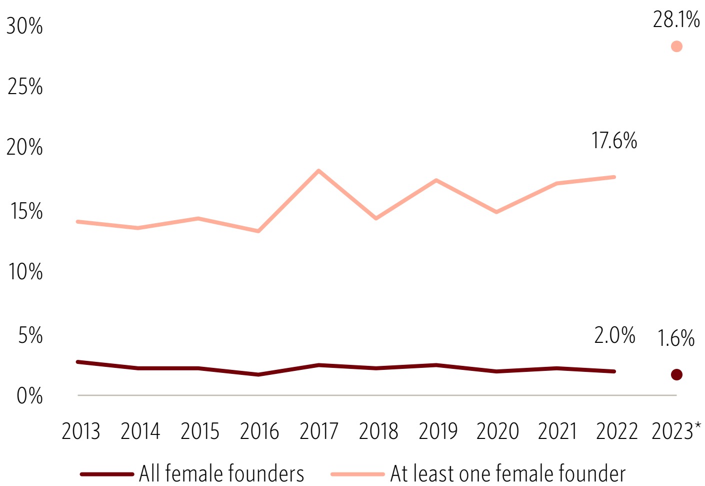
Companies with at least one female founder seeing record proportion of capital

Female-founded company deal value as a share of all US VC deal value



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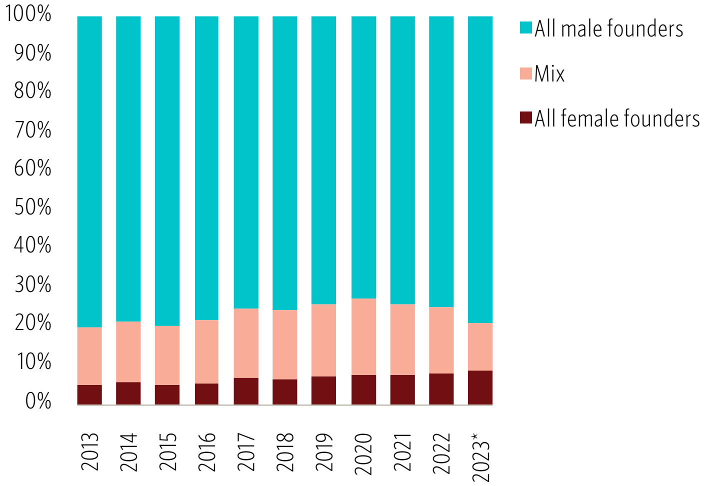
First-time financings still favor male founding teams

Share of US VC first-financings by founder gender



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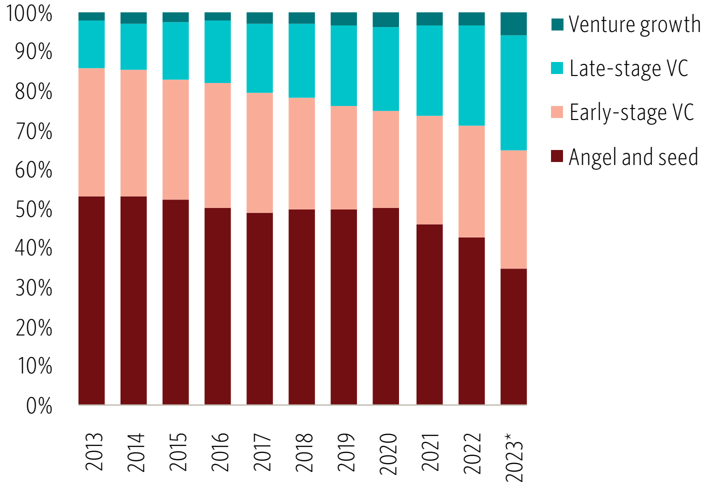
Venture growth outpacing 2022

Share of US VC deal count for female-founded companies by stage



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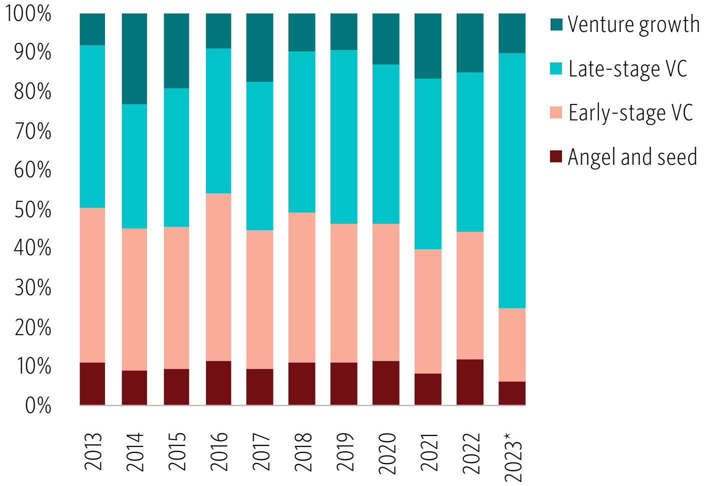
Late-stage deal value set to surpass record with strong H2

Share of US VC deal value for female-founded companies by stage



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New York deal count continues to outpace Bay Area

Top five US CSAs by deal count for companies with all-female founding teams (2019-2023)*

Combined statistical area	Deal count
New York	974
Bay Area	727
Los Angeles	471
Boston	193
Washington, DC	154

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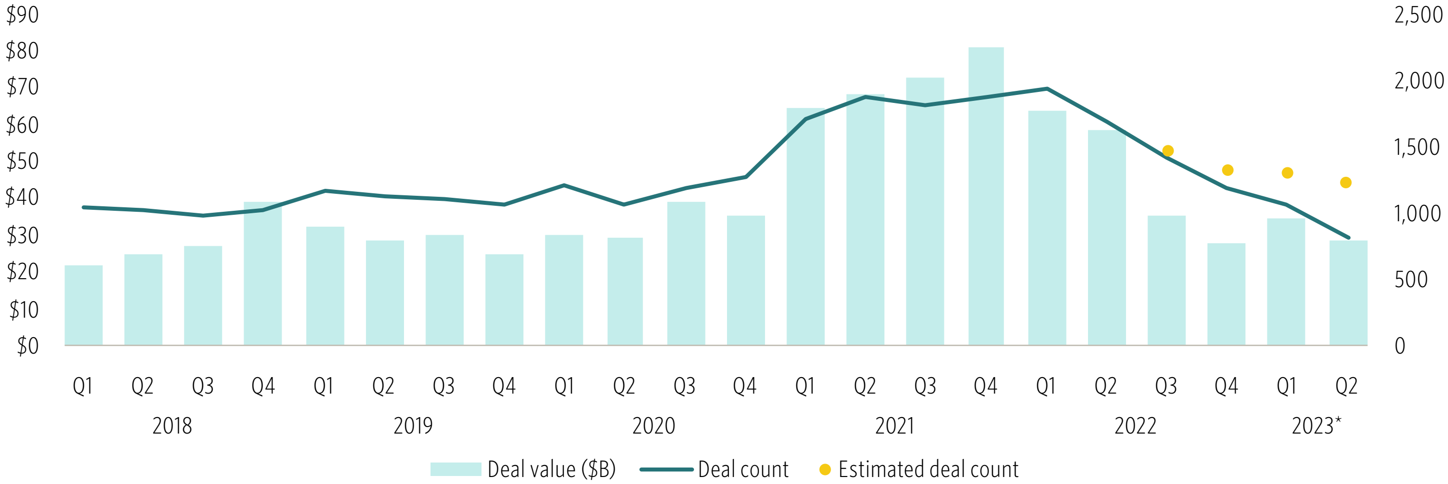
Nontraditional investors

Nontraditional investors' deployment to VC dips below $30 billion

US VC deal activity with nontraditional investor participation by quarter



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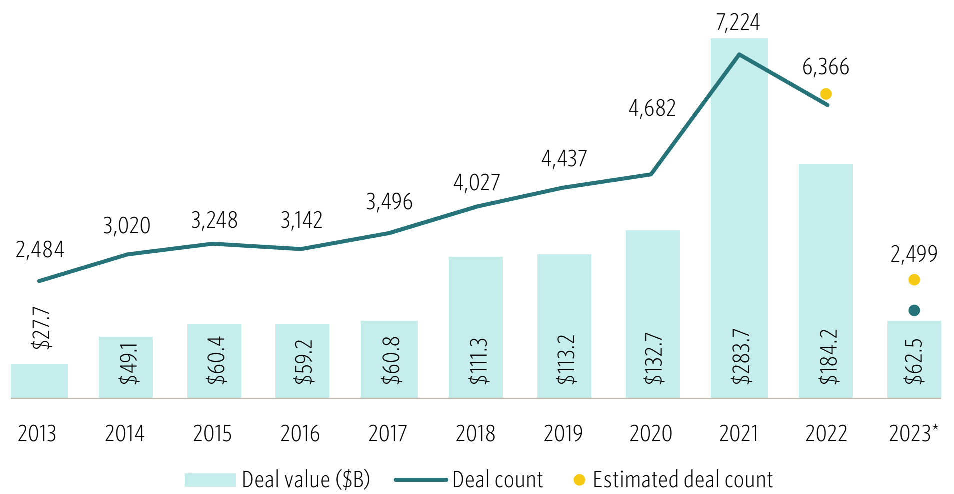
Nontraditional investors are particularly important for late- and venture-growth-stage startups, as they can provide substantial capital and strategically allocate their resources to capitalize on favorable risk profiles and potential returns. Through H1 2023, total deal value involving nontraditional investors amounted to $62.5 billion, accounting for 72.9% of the total deal value in the US VC market. This represents a decrease of nearly 10% compared with the participation rate of 81.7% observed in 2021.

The pullback of nontraditional investors has immediate consequences and is quickly observed in private markets, as it inherently limits the availability of capital for late- and venture-growth-stage startups. Consequently, these startups may have no choice but to attract new equity investors at flat or decreased valuations or pursue nondilutive forms of financing such as

Deal value participation roughly one-third of 2022 annual figure

US VC deal activity with nontraditional investor participation



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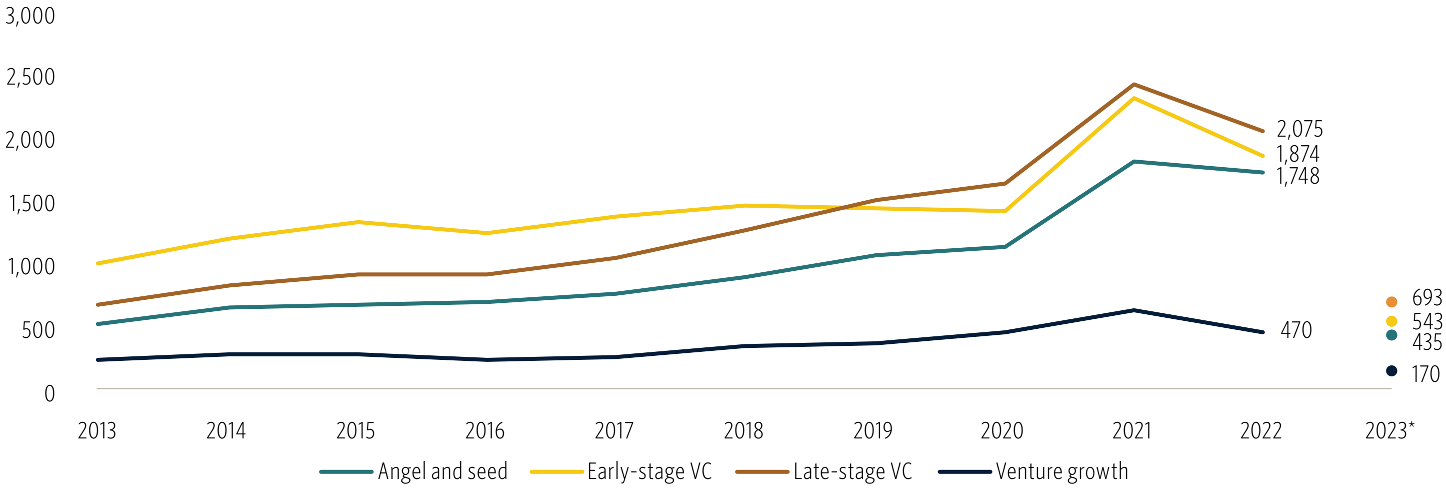
NTIs participate in just 170 venture-growth-stage deals through H1 2023

US VC deal count with nontraditional investor participation by stage



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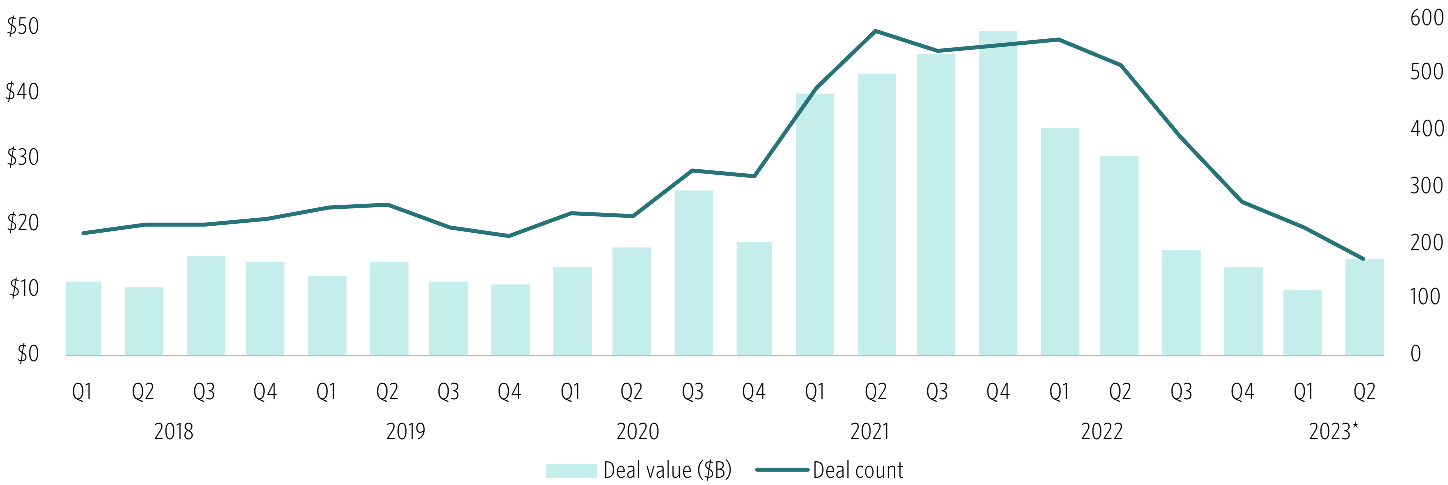
venture debt, which can be expensive and place an added burden on free cash flow. The latter option here, of course, is only possible for the highest-quality enterprises. Most nontraditional investors are drawn to VC due to its potential for lucrative financial returns. However, given the exit environment is the worst it has been in over a decade, many startups are struggling to generate any returns at all for their investors. Although nontraditional investors' percentage of deal value remained relatively high in Q2, the total number of deals involving nontraditional investors declined. For 2023 YTD, just 30.5% of US VC deals, or 2,499 deals, involved a nontraditional investor, which is notably lower than the 35.2% and 38.0% observed in 2022 and 2021, respectively. PE investor participation dropped from 15.3% of the annual deal count in 2022 to 12.6% in Q2 2023, while asset manager participation declined from 9.0% to 6.9% during the same period.

Crossover participation deal value ascends due to outsized deals

US VC deal activity with crossover investor participation by quarter



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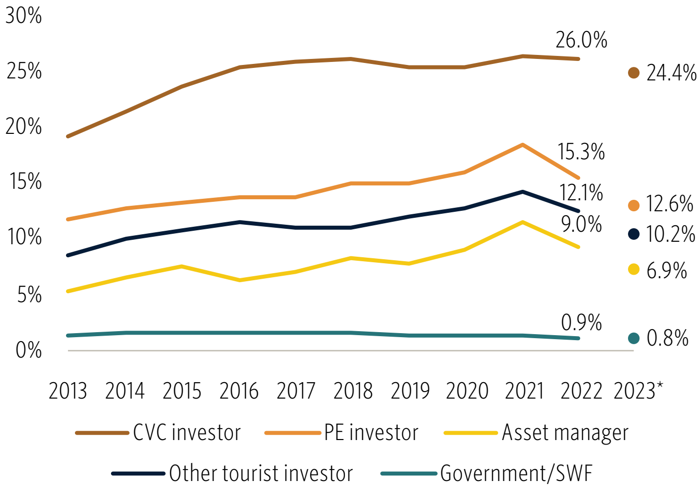
CVCs investors remain actively involved on a deal count basis

US VC deals with nontraditional investor participation as a share of all US VC deal count by investor type



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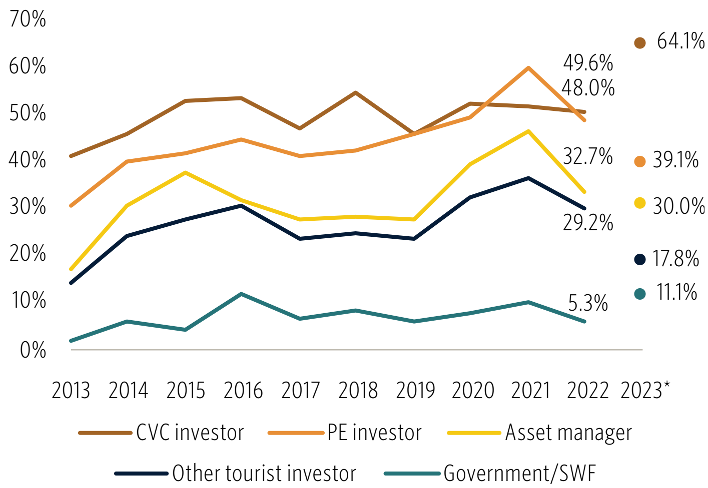
CVC deal value participation rises to highest percentage on record

US VC deal value with nontraditional investor participation as a share of all US VC deal value by investor type



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In contrast to other nontraditional investors, CVCs have maintained their activity level in terms of deal count. CVCs participated in 24.4% of all venture deals in Q2, experiencing a marginal decrease of approximately 1% compared with the annual participation rate observed in 2022 but remaining consistent with historical trends. As discussed in past research, we anticipate CVCs, which traditionally focus on early-stage startups due to strategic synergies and to more fiercely compete with peers, to continue to search for investment opportunities at a high rate. Declining startup valuations make these opportunities more attractively priced—and may result in an increased participation rate on an annual basis.

Despite this positive development, our data indicates that nontraditional investors displayed decreasing enthusiasm for VC during the first half of the year. Only 954 US venture deals, totaling $44.4 billion, were led by at least one nontraditional investor, which is roughly one-third of the 2,657 nontraditional-investor-led deals observed in 2022 (totaling $104.7 billion). The dwindling leadership and involvement of nontraditional investors is concerning for both startups and the venture ecosystem more broadly. As mentioned, these institutions have historically provided significant amounts of capital and expertise, and their absence makes it unlikely that we will reach the highs observed in 2021 and the first half of 2022.

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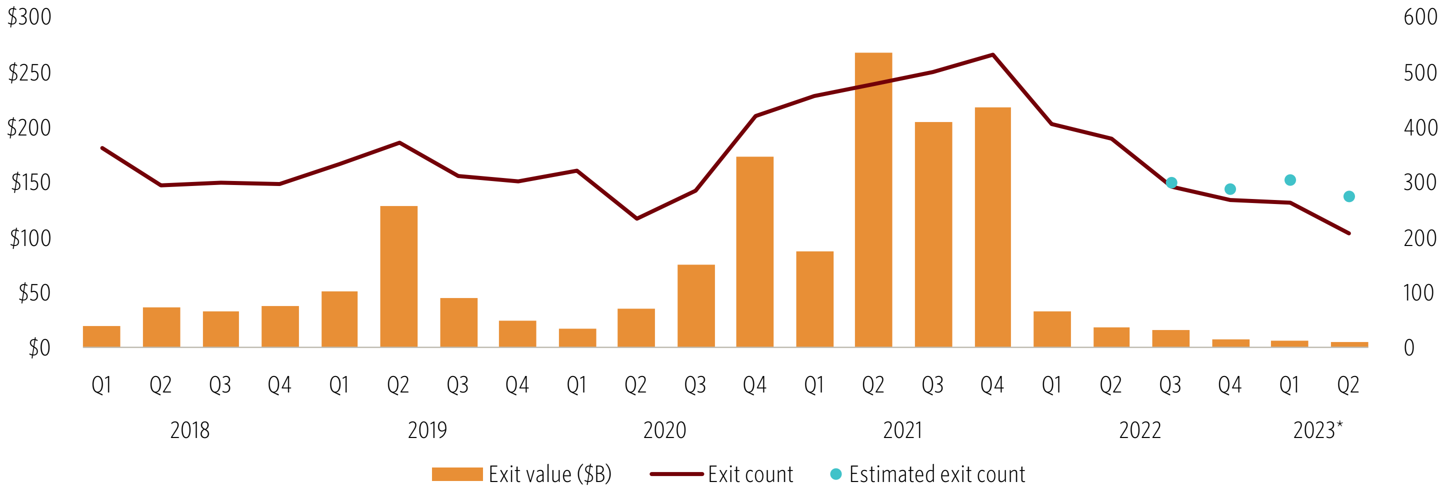
Exits

Q2 exit value declines to a decade low

US VC exit activity by quarter



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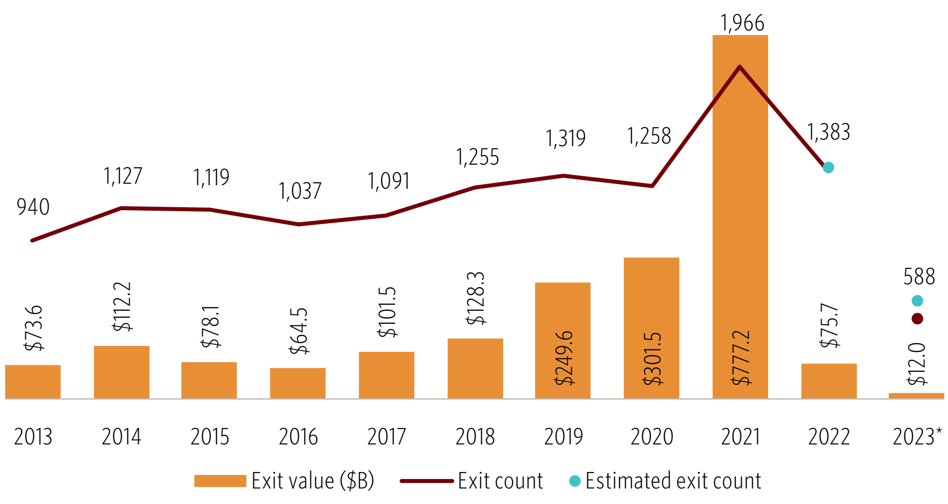
Immense amounts of capital are trapped in late- and venture-growth-stage startups hesitant to gamble on whether their financial performance can withstand the intense scrutiny of the public markets. The pullback of nontraditional investors, elevated interest rates, and persistent inflation continue to impact these late-stage companies' wherewithal to reach a successful exit and compel LPs to recycle capital into the VC ecosystem. Subsequently, through the first half of the year, we observed $12.0 billion in exit value generated from an estimated 588 exit events. The full-year figure will likely come in as the lowest of the decade.

In line with historical norms, acquisitions have accounted for the majority of exit events, but this year have also derived a majority of exit value. VCs continue to urge their

Exit count and value creation continue a lackluster performance through H1

US VC exit activity



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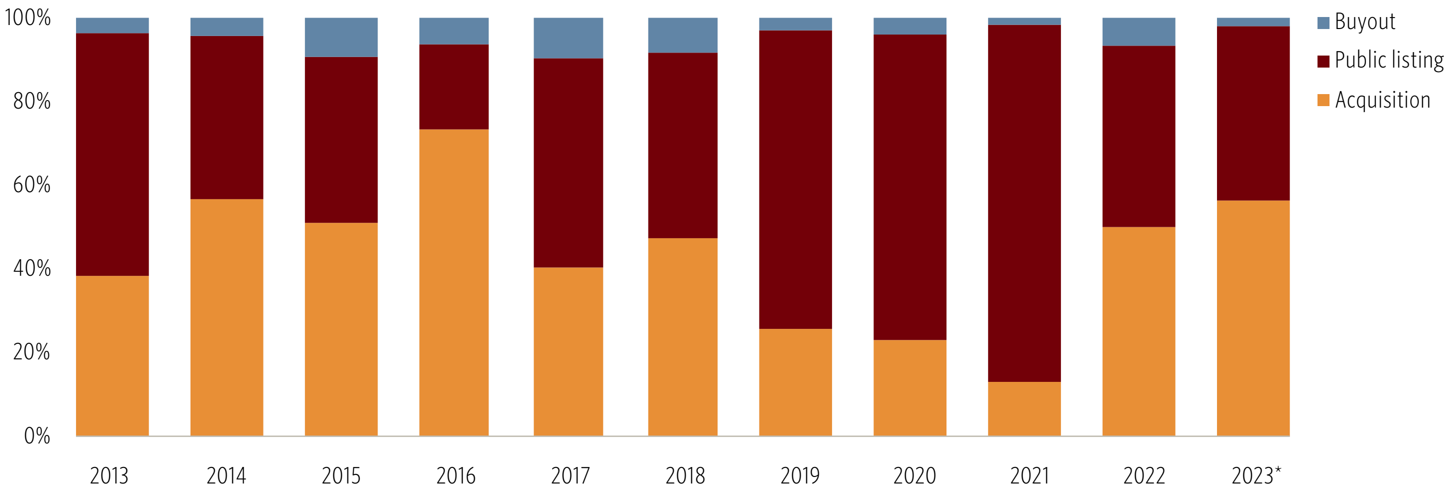
Majority of exit value YTD generated via acquisition

Share of US VC exit value by type



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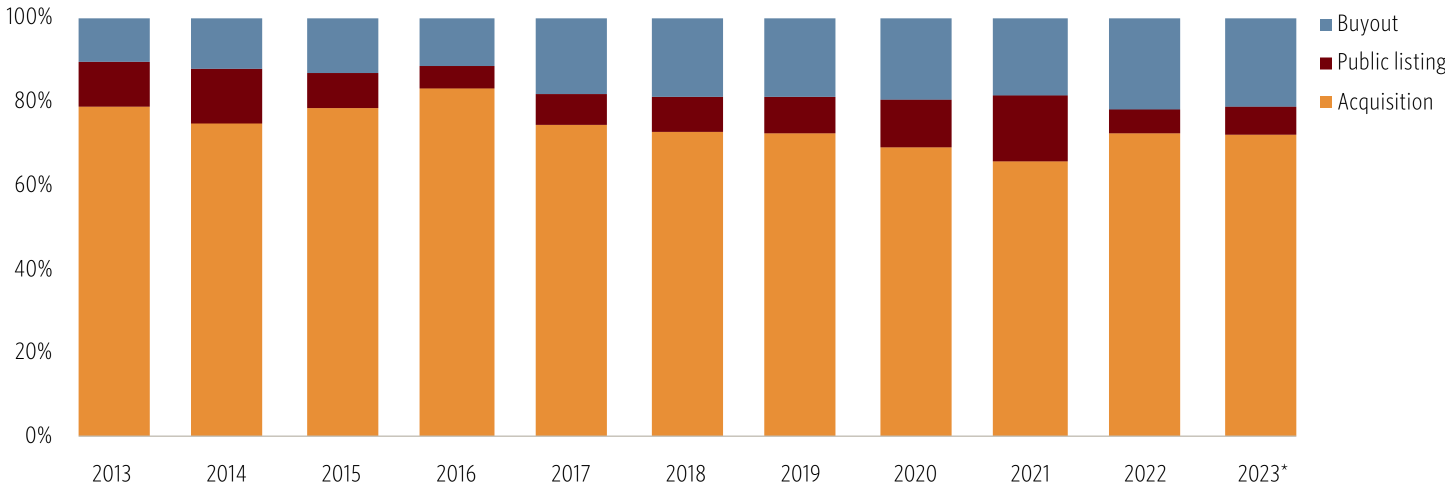
portfolio companies to seek liquidity, even if it means taking lower overall returns via an acquisition due to the challenging nature of the public markets. This narrative has played out in the data, with acquisitions generating $6.8 billion in exit value and capturing 56.5% of the total exit value generated YTD. Moreover, this push for liquidity has driven the median exit size via acquisition to a four-year high of $69.5 million. As highlighted in a recent analyst note, [M&A and CVC in an Economic Downturn](), the humbled IPO market has created opportunities for corporations to acquire promising startups at a discount. We expect the pace of acquisitions to pick up through the end of the year as more startups expend what's left of their cash runway and must either return to market to raise or hasten their exit timelines.

Despite the drab exit activity YTD, Mediterranean restaurant chain Cava's debut on the New York Stock Exchange has captured the attention of many

YTD share of exits via public listing inches above 2022

Share of US VC exit count by type



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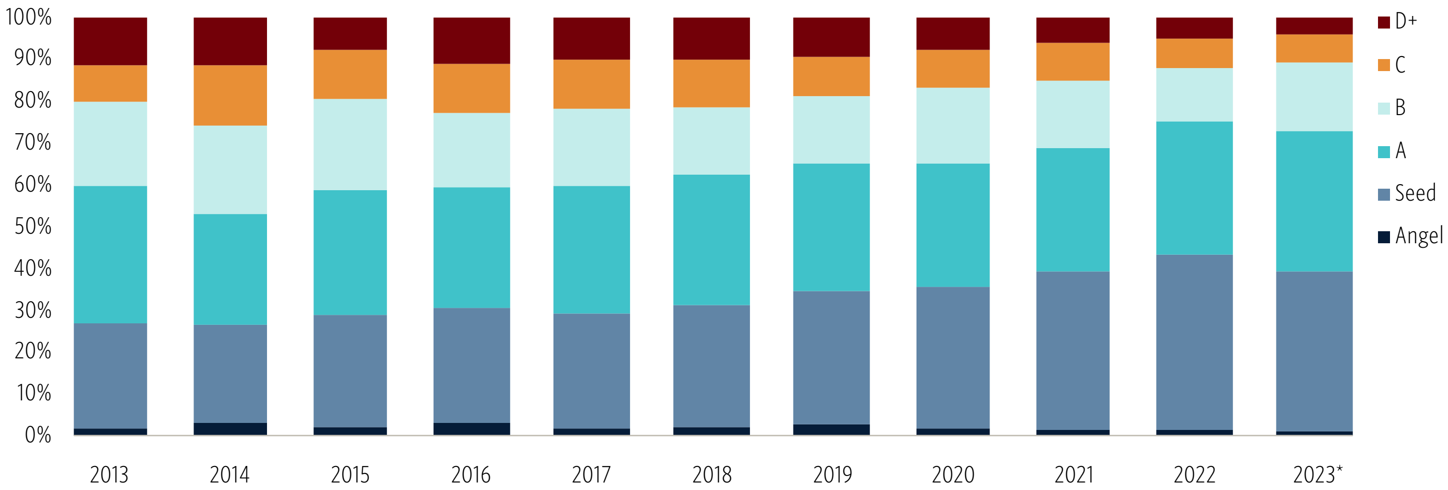
Small acquisitions account for growing proportion

Share of US VC round count by round series where next round is an exit via acquisition



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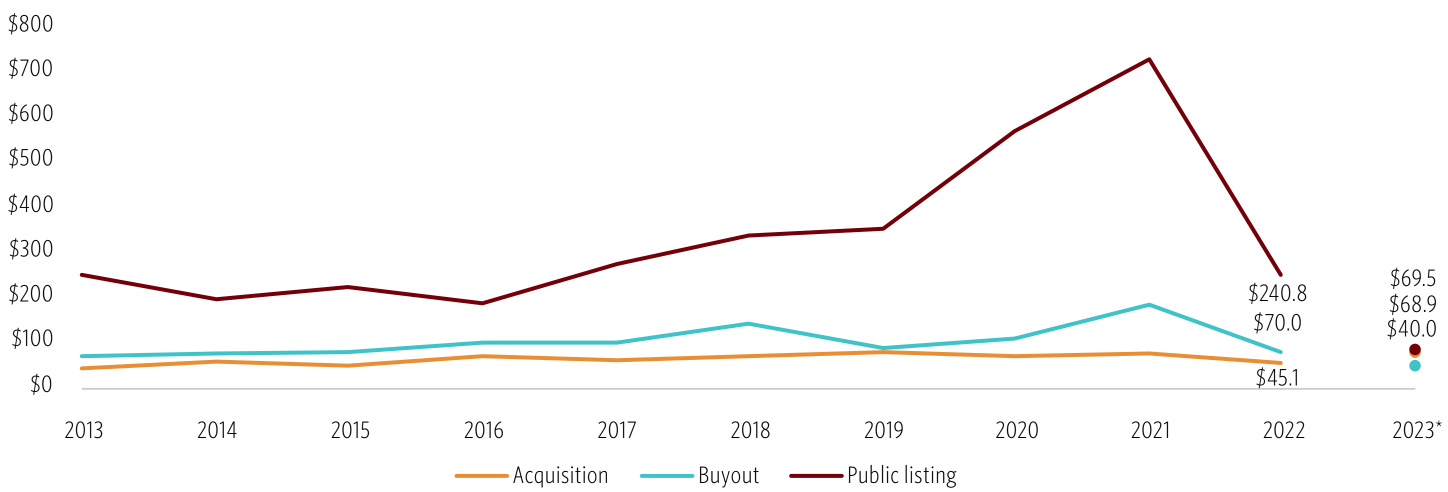
who hope that its success will pioneer a resurgence of the IPO market. Most of the IPOs seen since market headwinds picked up in early 2022 have been healthcare companies that require an injection of capital from public markets to fund clinical trials and research & development. Although Cava is not a tech-first business, meaning it is not a perfect comparison for the plethora of software and technology companies waiting on the IPO sidelines, its initial success in maintaining its stock price in the $36 to $48 range, well above the IPO price of $22, highlights how businesses with intended paths to profitability can allure investors. In order for an IPO resurgence to manifest for the broader VC market, startups will need to increase their focus on business fundamentals and appropriately price themselves reflective of their ability to achieve profitability.

Median exit size via public listing falls below $100 million for the first time in a decade

Median US VC exit value ($M) by type



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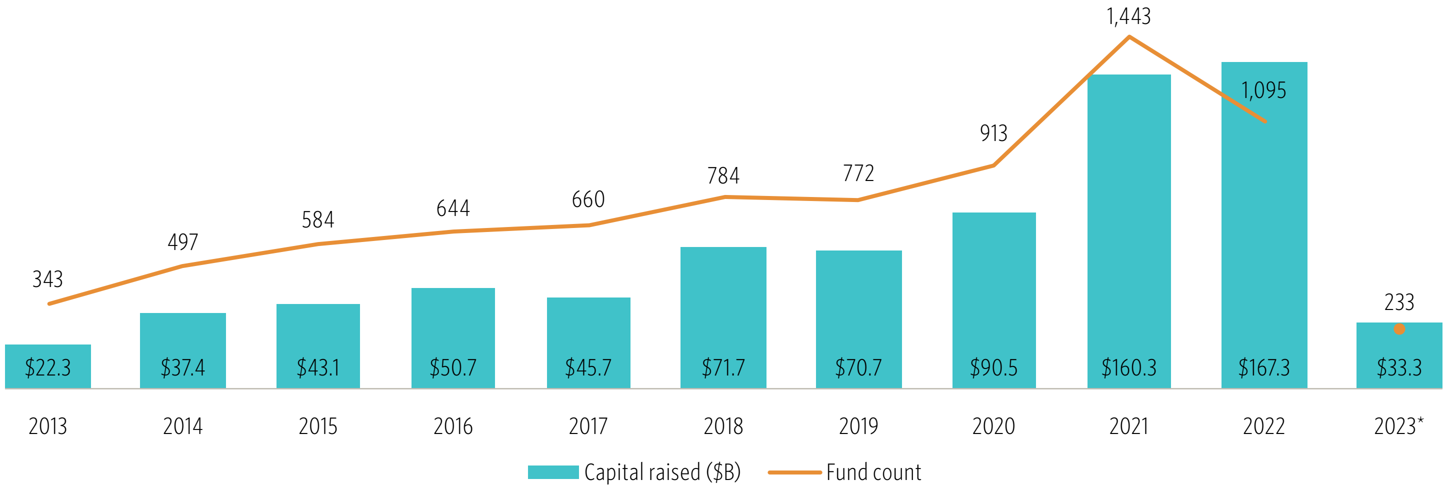
Fundraising

US VC capital raised on pace to set a six-year low

US VC fundraising activity



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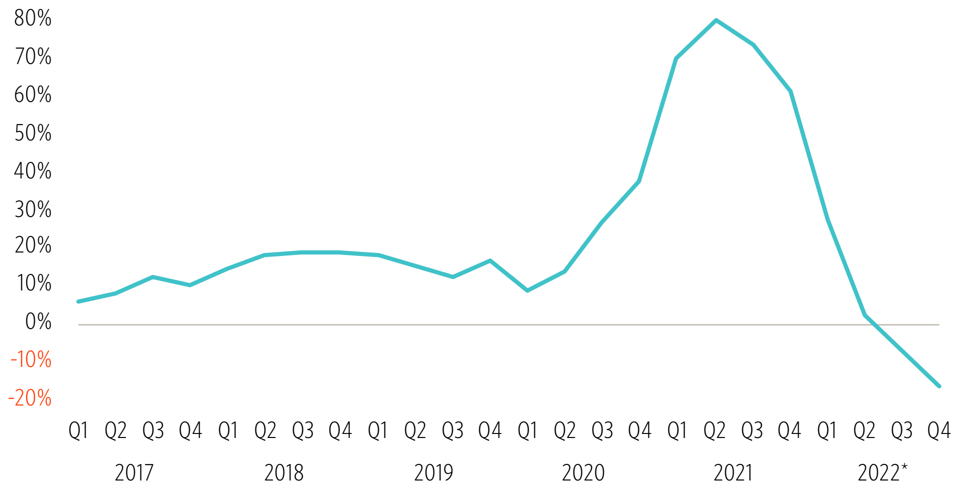
Fundraising activity continued to leave a sour taste in the mouths of GPs as a modest $33.3 billion was closed across 233 funds through Q2. The lackluster H1 has set a pace for the full-year fundraising figure to hit a six-year low. The frenzied pace of LP commitments in 2021 and early 2022 has fizzled out as a result of the overallocation to VC in 2021 and early 2022, slowing distributions, and the uncertain macroeconomic environment leaving many LPs wary of expected future returns from the venture strategy.

Emerging managers are feeling the brunt of the fundraising slowdown, capturing just $6.4 billion in commitments, or 19.1% of the total capital raised YTD. Many emerging-manager-led funds have not been in operation long enough to make large distributions back to LPs, and they likely invested at the peak of market valuations, thus creating concerns regarding overall performance now

One-year IRRs negative for first time since 2016

US VC rolling one-year IRRs



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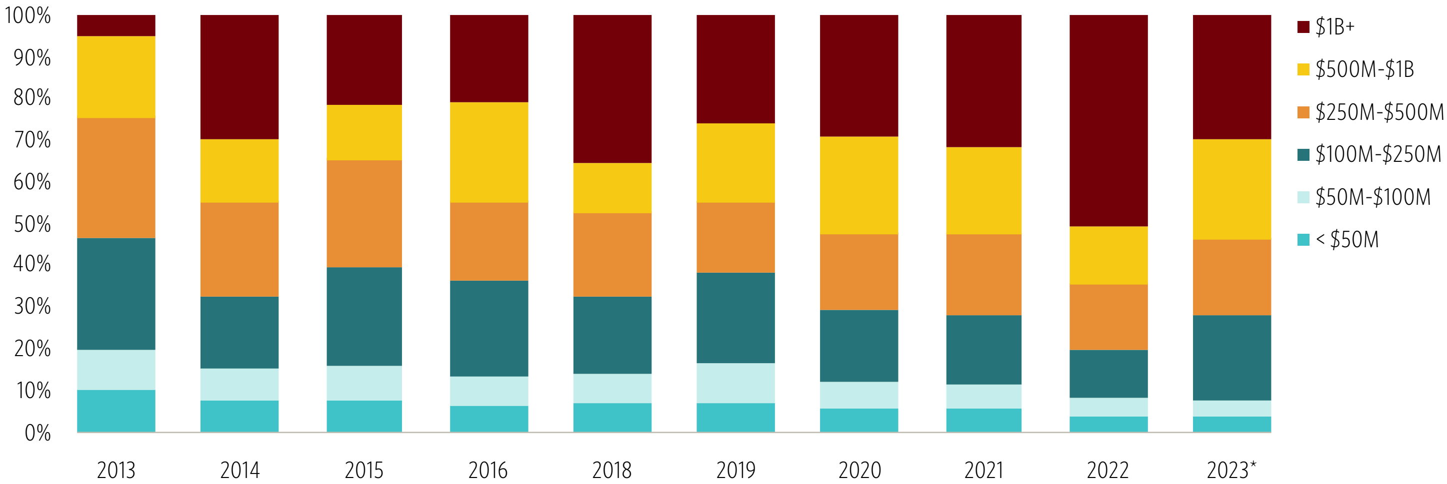
54% of capital raised committed to funds of $500M+

Share of US VC fund value by size bucket



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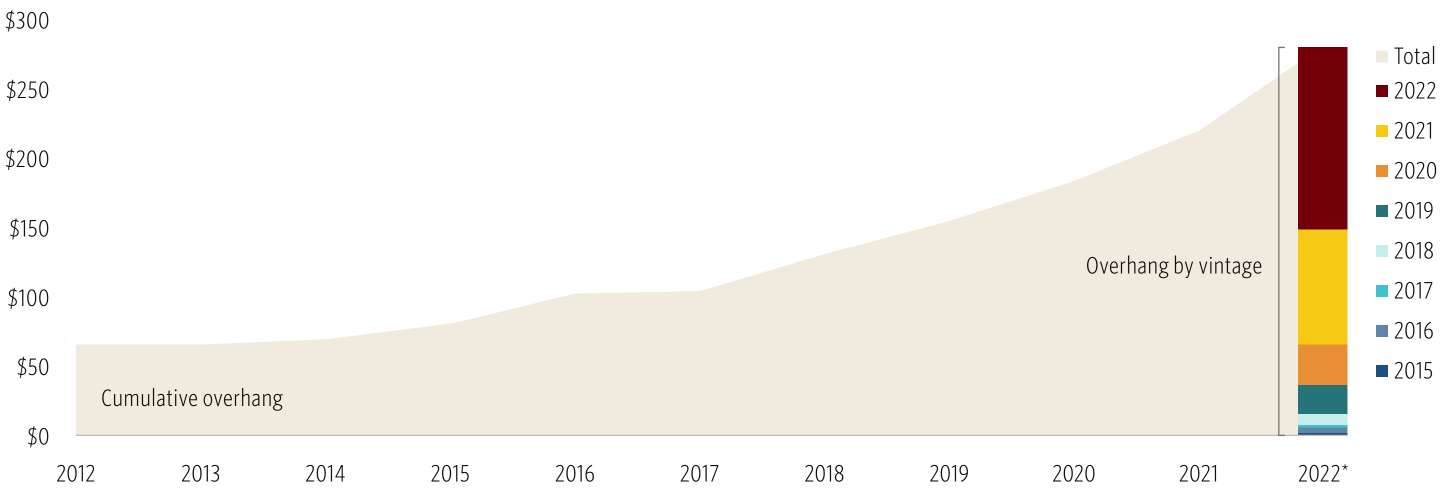
that valuations are being severely compressed. Additionally, to reach their target fund sizes, emerging managers are more reliant on high-net-worth individuals, who are more acutely pained by market fluctuations and consequently slow their fund commitments more dramatically than institutional investors such as pension funds and endowments. As a result, 2023 is poised to be the first year since 2016 to see emerging managers raise less than $20.0 billion.

First-time fundraising has seen an uptick since our [Q1 2023 PitchBook-NVCA Venture Monitor](), with 36 first-time funds and $3.2 billion raised added to our dataset in Q2. Yet this ray of hope is obscured by the fact that one-fourth of the first-time funds closed YTD had commitments over $100 million, an abnormally large fund size for newly minted VCs. The ability to raise outsized amounts of capital is largely attributable to the pedigree of the VC's founding partners. For VCs without

US VC record dry powder remains high due to sidelined investor capital

US VC dry powder ($B) by vintage



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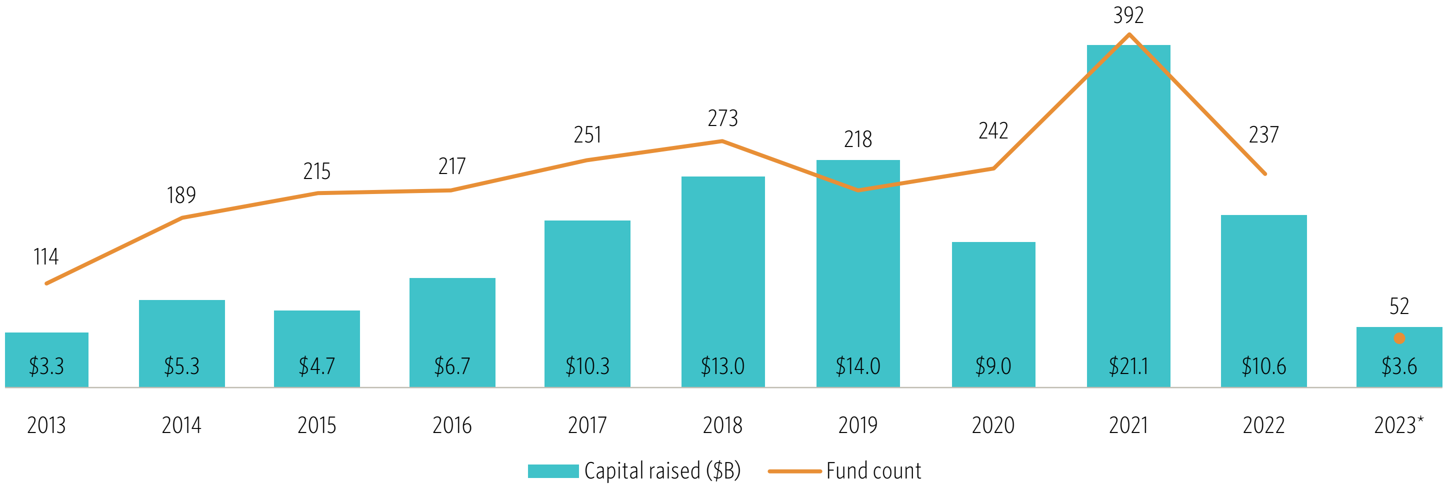
25% of first-time funds closed YTD account for 81% of fund value

US VC first-time fundraising activity



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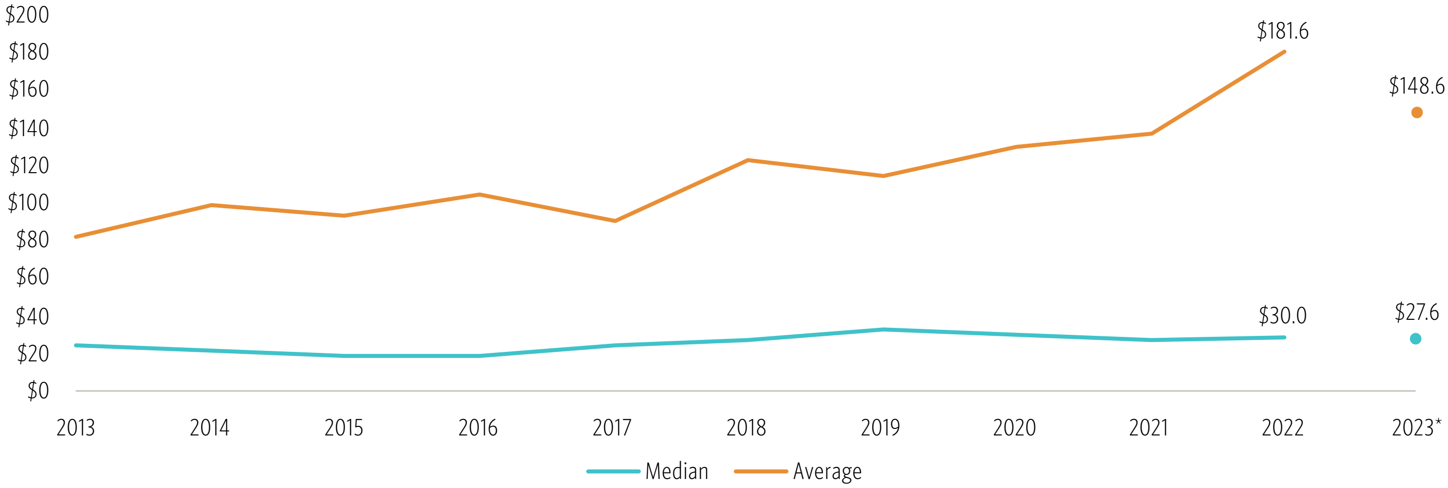
robust experience, track records, and networks to instill confidence in LPs, many emerging managers will likely stall fundraising efforts for the remainder of 2023 and into 2024.

In contrast to the fundraising slowdown, the US VC dry powder figure remains elevated at $279.8 billion and will likely remain elevated through the end of 2023. $170.5 billion, or 60.9%, of this dry powder is concentrated in mega-funds—those with $500.0 million or more in commitments—many of which have slowed their dealmaking activity in response to market volatility.

The large amount of dry powder is meaningful in that it can be deployed in the future, but the catalysts for this drawdown will be access to liquidity, subsiding of headwinds, and a return of mega-rounds en masse.

Average fund size declining

Median and average US VC fund values ($M)



PitchBook-NVCA Venture Monitor
*As of June 30, 2023

Q2 2023 league tables

*Most active investors angel and seed**

1	Pioneer Fund	38
2	Goodwater Capital	32
3	10X Capital	25
4	Y Combinator	24
5	SOSV	21
6	Elevate Ventures	19
7	Triangle Tweener Fund	17
7	Alumni Ventures	17
9	Service Provider Capital	15
10	Sequoia Capital	14
10	Soma Capital	14
10	Gaingels	14
10	IndieBio	14
14	Plug and Play Tech Center	13
15	Everywhere Ventures	12
16	Connecticut Innovations	11
17	Rebel Fund	8
18	Liquid 2 Ventures	7
18	FJ Labs	7
18	500 Global	7
21	Hax	6
21	Unusual Ventures	6
21	Michigan Rise	6
21	Kevin Moore	6
21	Correlation Ventures	6

PitchBook-NVCA Venture Monitor
*As of June 30, 2023

*Most active investors early stage**

1	Sunstone Management	14
2	ImpactAssets	11
2	FJ Labs	11
4	Sequoia Capital	9
4	Lair East Labs	9
4	Andreessen Horowitz	9
7	StartX (US)	8
7	New Enterprise Associates	8
9	Alexandria Venture Investments	7
9	Boost VC	7
11	Y Combinator	6
11	Fortified Ventures	6
11	Soma Capital	6
11	Raptor Group	6
11	Alumni Ventures	6
16	Village Global	5
16	Realm Capital Ventures	5
16	SV Angel	5
16	Pioneer Fund	5
16	Social Leverage	5
16	Pear	5
16	Lightspeed Venture Partners	5
16	Keiretsu Forum	5
16	Eberg Capital	5
16	GV	5
16	Bling Capital	5

PitchBook-NVCA Venture Monitor
*As of June 30, 2023

*Most active investors late stage**

1	Alumni Ventures	14
2	FJ Labs	11
3	SOSV	10
3	Gaingels	10
5	Keiretsu Forum	9
6	ImpactAssets	8
6	Eastward Capital Partners	8
6	Andreessen Horowitz	8
6	10X Capital	8
10	TEDCO	7
10	500 Global	7
12	Wellington Management	6
12	Tiger Global Management	6
12	Revolution/ROTR	6
12	Norwest Venture Partners	6
12	Plug and Play Tech Center	6
12	Khosla Ventures	6
12	General Catalyst	6
12	Connecticut Innovations	6
12	GV	6
21	Felicis	5
21	Partnership Fund for New York City	5
21	Sequoia Capital	5
21	Insight Partners	5

PitchBook-NVCA Venture Monitor
*As of June 30, 2023

*Most active investors growth stage**

1	Keiretsu Forum	5
2	ImpactAssets	4
2	HBM Healthcare Investments	4
4	FJ Labs	3
4	Norwest Venture Partners	3
4	Michigan Rise	3
4	Thrive Capital	3
4	Salesforce Ventures	3
4	Arboretum Ventures	3
4	Energy Impact Partners	3
4	Realm Capital Ventures	3

PitchBook-NVCA Venture Monitor
*As of June 30, 2023

Methodology

Deals

We include equity investments into startup companies from an outside source. Investment does not necessarily have to be taken from an institutional investor. This can include investment from individual angel investors, angel groups, seed funds, VC firms, corporate venture firms, corporate investors, and institutions, among others. Investments received as part of an accelerator program are not included; however, if the accelerator continues to invest in follow-on rounds, those further financings are included. All financings are of companies headquartered in the US, with any reference to "ecosystem" defined as the combined statistical area (CSA). We include deals that include partial debt and equity.

Angel and seed: We define financings as angel rounds if there are no PE or VC firms involved in the company to date and we cannot determine if any PE or VC firms are participating in the round. When it is reported by a government filing and the deal amount is below $1 million and investors are unknown, it is defined as angel. In addition, if there is a press release that states the round is an angel round, and no institutional investors are involved, it is classified as such. Finally, if a news story or press release only mentions individuals making investments in a financing, it is also classified as angel. As for seed, when the investors and/or press release state that a round is a seed financing, or it is between $1 million and $10 million as reported by a government filing and investors are unknown, it is classified as such.

Early stage: Rounds are generally classified as Series A or B (which we typically aggregate together as early stage) either by the series of stock issued in the financing or, if that information is unavailable, by a series of factors, including the age of the company, prior financing history, company status, participating investors, and more.

Late stage: Rounds are generally classified as Series C or D (which we typically aggregate together as late stage) either by the series of stock issued in the financing or, if that information is unavailable, by a series of factors, including the age of the company, prior financing history, company status, participating investors, and more.

Venture growth: Rounds are generally classified as Series E or later (which we typically aggregate together as venture growth) either by the series of stock issued in the financing or, if that information is unavailable, by a series of factors, including the age of the company, number of VC rounds, company status, participating investors, and more.

Nontraditional investors: "CVC" includes rounds executed by established CVC arms as well as direct equity investments by corporations into VC-backed companies. "PE" includes VC deals by investors whose primary classification is PE/buyout, growth, mezzanine, or other private equity. "Crossover" investors are a subset of nontraditional investors—specifically asset managers, hedge funds, mutual funds, and sovereign wealth funds—that have been active in VC investment across any stage. They are referred to as crossover because these investors are likely to be participating at the late stages directly prior to an exit.

Venture debt: The venture debt dataset is inclusive of all types of debt products raised by VC-backed companies, regardless of the stage of company. In mixed equity and debt transactions, equity is excluded when the amount is of known value. Financings that are solely debt are included in this dataset, though not incorporated into the deal activity dataset used throughout the report. Mixed equity and debt transactions will be included in both datasets.

Exits

We include the first majority liquidity event for holders of equity securities of venture-backed companies. This includes events where there is a public market for the shares (IPO) or the acquisition of majority of the equity by another entity (corporate or financial acquisition). This does not include secondary sales, further sales after the initial liquidity event, or bankruptcies. M&A value is based on reported or disclosed figures, with no estimation used to assess the value of transactions for which the actual deal size is unknown. IPO value is based on the pre-money valuation of the company at its IPO price. One slight methodology update is the categorical change from "IPO" to "public listings" to accommodate the different ways we track VC-backed companies' transitions to the public markets. To give readers a fuller picture of the companies that go public, this updated grouping includes IPOs, direct listings, and reverse mergers via SPACs.

Fundraising

We define VC funds as pools of capital raised for the purpose of investing in the equity of startup companies. In addition to funds raised by traditional VC firms, PitchBook also includes funds raised by any institution with the primary intent stated above. Funds identifying as growth-stage vehicles are classified as PE funds and are not included in this report. A fund's location is determined by the country in which the fund's investment team is based; if that information is not explicitly known, the HQ country of the fund's general partner is used. Only funds based in the United States that have held their final close are included in the fundraising numbers. The entirety of a fund's committed capital is attributed to the year of the final close of the fund. Interim close amounts are not recorded in the year of the interim close.

PitchBook nvca

A perfect partnership: PitchBook and the National Venture Capital Association

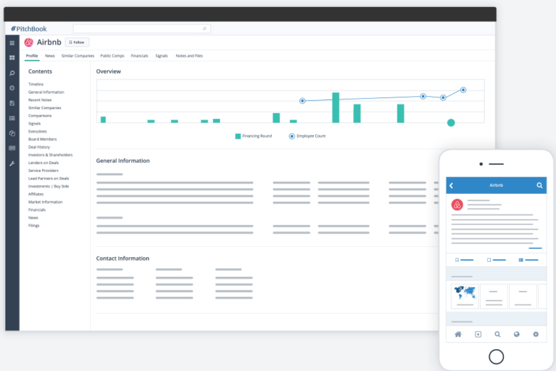
Why we teamed up

NVCA is recognized as the go-to organization for venture capital advocacy, and the statistics we release are the industry standard. PitchBook is the leading data software provider for professionals in venture capital, serving more than 4,000 customers across the private markets. Our partnership with PitchBook empowers us to unlock more insights on the VC ecosystem and better advocate for our evolving industry.

The PitchBook-NVCA Venture Monitor

Informed by PitchBook data, our quarterly Venture Monitors dive deep into venture capital activity and deliver insights to inform your investment strategy. PitchBook data also bolsters our annual year-in-review publication.

THE PERKS OF PARTNERSHIP



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As an NVCA member, your free access to the PitchBook Platform includes five advanced searches and five profile views per month.

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