

EUROPEAN VENTURE SENTIMENT

REPORT Q3

Investors expect difficult times to continue

The COVID pandemic continues to have a negative impact on the wider economy and the venture ecosystem is not an exemption. The European Venture Sentiment Index for Q3 was nearly unchanged compared to the previous quarter, with a slightly negative outlook for Q4.

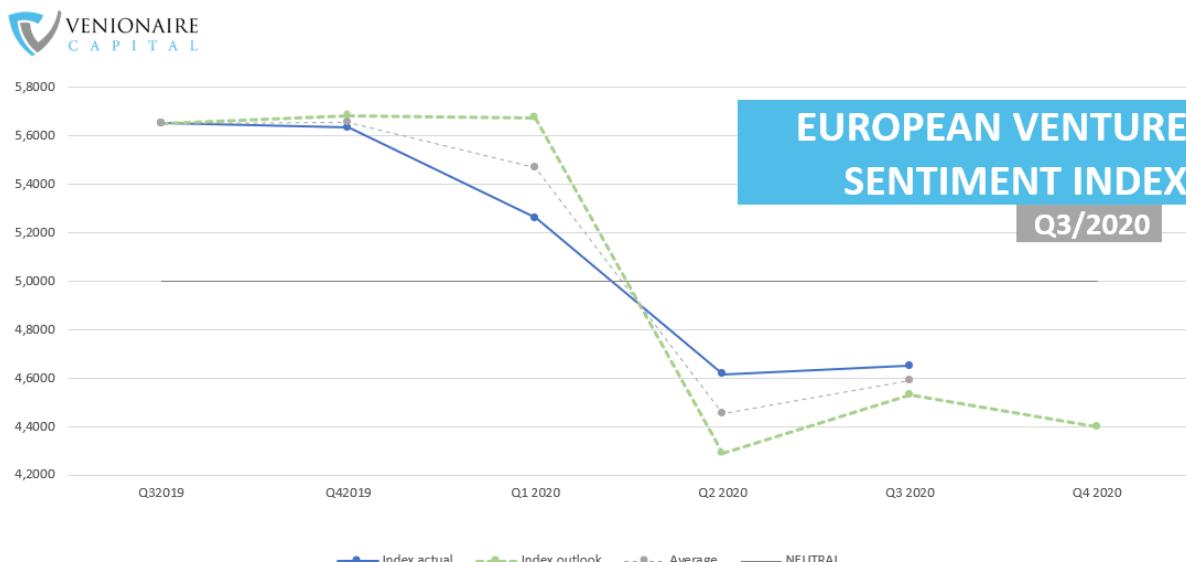
"We anticipate that European investors expect a challenging fundraising environment, focus on existing investments, and scrutiny of any potential new opportunities. Government programs continue to play a large role. That said European countries get very different scores from the ecosystems when it comes to efficiency of such programs. Germany performs strong, while other countries struggle to deliver. The overall European outlook is slightly negative, as additional pressure from a second wave is expected."

Berthold Baurek-Karlic, Venionaire Capital

The outlook continues to trend slightly downwards until the rest of the year, reflecting fears about a possible second wave of the pandemic in the colder months of the year.

Sentiment index stable, investors focus on portfolio companies

The COVID-19 pandemic is still front and center on everyone's mind, being the most prevalent topic in most of the conducted surveys and interviews. The European Venture Sentiment Index has remained largely unchanged, going from 4.62 in the previous quarter to 4.65 in Q3 2020. Investors also seem to be getting better at navigating and predicting the crisis, as the spread between the predicted score and the actual one is the narrowest since the crisis began. Nevertheless, for the second quarter in a row the index is slightly higher than predicted in the previous period, reflecting



pessimism still present among venture investors.

We have observed an increase in investment activity in Q3, due to portfolio companies experienced higher burn-rates, while suffering from weaker sales. New investments decreased. Investors have taken advantage of “good deals” and invested at lower valuations, over all valuations where reported to be stable overall. The fear of a depreciation in values did not become reality. Given the uncertainty investors stay alert and will remain focused on existing portfolio companies. New investments continue to be viewed as highly opportunistic, and “cherry picking only” seems to still be the prevalent modus operandi.

A slight drop-in activity is expected in the next quarter, as investors predict bargain deals to dry up. The fundraising environment also continues to be very difficult, which further supports the risk-off approach. On a more positive note, deal flow generation and evaluation has improved compared to the last quarter, and investors cite better remote working conditions and getting used to the “new normal” as the primary reasons.

Negative outlook for Q4 2020, second wave fears

The outlook for Q4 goes even deeper into negative territory, falling to 4.4 points, which is lower than both the projected and the actual score for the current quarter. Fears of the second wave of the Coronavirus and possible ensuing lockdowns are

omnipresent, which would drag the world economy into an even deeper recession. Because of this, the environment for new investments will still be difficult, with most investors still assuming a defensive stance and focusing on their existing portfolio. In comparison, startups themselves are more positive, reporting optimism they can succeed in the face of a second wave due to adaptive business models, digitalization, and adjusting to remote work practices.

Sectors uneven, government programs expiring

Just like before, the crisis is not hitting everyone equally. While the travel, transportation, and hospitality industries are still under massive pressure, other digital and high-tech startups are largely unaffected. Investors have claimed that by this point nearly all startups payed a tribute to the COVID crisis, even winners had to ramp up resources to deliver on exploding demand (which is a challenge of its own). Some companies managed to adapt their business model, others acquired or merged with peer, change is omni present these days fund managers report.

On another front, many national government and Europe-wide startup support programs are coming to an end, which is feared to endanger destabilized companies and the often “weak” ecosystems in developing countries of the European Union. In countries such as Austria, Spain, or Poland, there was little continuous support after the initial push, which is making investors cautious and

restrictive for further investments. On the other hand, Germany, as one of the largest European startup hubs, has seen abundant government support, as have most Nordic countries. This has most likely had a great impact on the stabilization of the sentiment index in Q3. The programs on the European level are continuing to be a mixed bag, with startups often complaining about complexity and bureaucracy. Clear instructions on who can apply where and for what, would be happily welcomed by the entire ecosystem.

To sum up, even though the venture sentiment has largely stabilized since the sharp drop between Q1 and Q2, we still find ourselves in negative territory. Investors expect a further (albeit modest) decline in Q4, mainly fueled by fear of the second wave of the COVID-19 pandemic, and expiration of government support programs.

Methodology

Over seventy highly experienced investors (business angels, (corporate) venture fund managers and family offices) from ten European countries were interviewed in August and September 2020 as part of the European Venture Sentiment Survey, conducted by Venionaire Capital. Based on a quarterly recurring survey, Venionaire Capital collects answers from a focus group in the form of computer-assisted personal interviews, and of a much smaller control group to assess the indices. Those datasets are collected in two waves and finally merged. In both groups, Venionaire has aligned similar sets of investors, ranging from business angels to large corporate venture

units as well as early- to later-stage venture capital funds from all over Europe (incl. Switzerland and the UK).

The indices for current sentiment and projected outlook are weighted indices, with emphasis on the ability / willingness of investors to invest, the perception of startup valuations and the quality of deal-flow.

COMPARABILITY

Sentiment surveys and indices are nothing new. They have been around for decades to quantify how a certain group of people feel about a market or economy. One of the most notable examples is the Consumer Confidence Index (CCI), which provides an indication of future consumption and saving of households. There are also surveys that focus on a specific market, or even an individual security. How can the results of these market sentiment surveys help market participants?

Let's look at the venture capital industry. This general economic information can greatly benefit both the investor and startups within a market. Investors can compare their own views and opinions to those of the general market or across different geographical regions and industry verticals. This will help them to adjust their investment behavior. Startups can use this information, when growing their business internationally, when they prepare for fundraising or to slow down their business (return to bootstrapping – ahead of time), if the economic environment worsens. Market sentiment indicators are important for us in all industries and markets.

Nevertheless, there is a limited number of market sentiment indices for the venture capital or startup market available, which we found useful to work with.

Most indices available focus on a specific region, investors group or industry. Take EIF's VC Survey, which targets a highly professional group of regulated investors across Europe but does not take accelerators or business angels into account. Our partners of Deutsche Börse Venture Network conducted a great report on market sentiment during the COVID-19 pandemic. It offers great insights, but it was a onetime publication.

We have developed our own "European Venture Sentiment Index", which shows in one simple number the general state of sentiment today and shows the current outlook in a second number.

EUROPEAN INVESTOR SENTIMENT INDEX

The index is based on feedback from different economic regions, as well as startup sectors and reflects the general European Venture Sentiment. The methodology of the index was designed by Venionaire Capital in mid-2019. The project was led by its founder and managing partner, Berthold Baurek-Karlic, a serial entrepreneur and leading venture capital expert from Vienna, Austria. Having started his career in the statistics department of the Austrian Central Bank (OeNB) he is a great supporter of data driven analysis.

ABOUT



BERTHOLD BAUREK-KARLIC

CEO & FOUNDER, VENIONAIRE CAPITAL

Berthold Baurek-Karlic is the founder and managing director of Venionaire Capital, specialized in M&A and venture capital. His group also includes the investment company MOTEC VENTURES (motec.vc) and the software provider DEALMATRIX (dealmatrix.com).

He is also the founder and secretary general of the Business Angel Institute (businessangelinstitute.org), board member of the European Super Angels Club (superangels.club), expert partner of various accelerators and consultants of various venture funds, and board member of the Austrian Private Equity and Venture Capital Association (avco.at), as well as external consultant in the EU programs Horizon2020 (today Horizon Europe) and Innovation Radar.

As a passionate blogger (www.baurek-karlic.at), he writes regularly on various topics related to angel and venture investments, startups, and future technologies.