



EUROPEAN INVESTOR SENTIMENT INDEX

Quaterly Survey

Q1/2023

April 18, 2023

BANKING CRISIS AND HIGH INFLATION UNDERMINE EUROPEAN VC RECOVERY IN Q1 2023.

Q1 2023 was expected to be the continuation of the European economy recovery, as highlighted by the International Monetary Fund report after three macroeconomic events shook European economics (WEF, 2023). The war in Ukraine, rising inflation, and the energy crisis. Despite signs of recovery in Q4 2022, in Q1 2023 Venture investment was faced with a banking crisis as well, which affected several institutions, including vital Silicon Valley Bank and Credit Suisse.

Silicon Valley Bank (SVB) was a banking institution that specialized in issuing financing to startups, primarily in the technology sector. The bank has collapsed due to a combination of factors, including mismatch in Asset Liability Management (ALM) expressed in majorly investing in long-term bonds with fixed interest rate, which were drastically increased by the central banks to defeat high inflation. As a result, the bond portfolio of the bank lost significant value. This resulted in a "bank run", which led to SVB being unable to meet its obligations, ultimately leading to its collapse. After the bank was shut down in March 2023, market participants considered the high exposure to the startup technology sector as a main cause of the bank failure due to inability of SVB to hedge its high bond exposure with its deposits.

However, another large bank has collapsed - the European Swiss-based bank Credit Suisse, which has caused a significant impact on the European economy and the European VC market. The bank suffered massive losses as a result of its exposure to similar long-term bonds with fixed interest rates as well as its involvement in the Greensill Capital and the Archegos Capital Management scandals. These events led to significant financial losses for Credit Suisse and a loss of confidence among investors, which, in turn, resulted in the acquisition by UBS. Despite the acquisition having already been executed, we expect to hear about it further in the following quarter, as it may raise many concerns regarding the difference in the market and sale values for the acquisition.

Even though the banking crisis started in the US, it had a strong effect on European venture ecosystems. Many VC firms and startups held their deposits in the damaged banks. Their collapse had significantly undermined faith in the Venture Capital market in Europe. As a result, we observe more of a "cherry-picking" attitude from investors. Meanwhile, due to lower economic activity, many VC firms are focused on supporting their portfolio companies rather than searching for new opportunities, which can lead to investors missing out on a larger number of opportunities, that, in turn, would represent a significant threat to the entire VC market, leading to many potentially successful startups lacking liquidity and then going bankrupt.



The European Venture Capital market was expected to continue its recovery in Q1 2023. However, after the ECB has been raising the deposit interest rates during the quarter, followed by the collapses of SVB, Silvergate, and Credit Suisse, it became clear that distress in the economy generally, and particularly in the PE and VC markets, is getting exacerbated. We observed both institutional and private investors indicating slightly lower interest in venture capital investments in Europe, which is, in fact, a global phenomenon rather than local. Nevertheless, this quarter we observed a higher concentrated European VC investment market with the UK, France, and Germany constituting 62.6% of the entire market, which could be a sign of the weakness of smaller venture ecosystems in Europe.

We have noticed that fundraising has become even more challenging and complex, especially for early growth stage startups, compared to the previous quarter. Both private and institutional investors have been exceptionally careful with adding new startups to their portfolios. Following the trend that started at the end of 2022, VC players focus on supporting their existing portfolio and allocate the majority of their funds to maintain and enhance fundraising for their existing portfolio winners. Most experts in our interviews argue that this quarter's actual point is likely to be the bottom for 2023. As a result, survey respondents believe that the European venture ecosystem will revive, building on the recovery attempts that began in Q4 2022. They predict that this quarter marked the bottom for 2023 and that the venture market will begin to regain momentum going forward.

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To prevent a domino effect and to contain inflation, the ECB raised interest rates by 0.5%, thereby reaching the 3% level in March 2023 (European Central Bank, 2023).

Although the ECB was not expected to increase the deposit interest rate due to the banking crisis, the market reacted relatively positive with positive moves in the German DAX and French CAC 40 indexes.

Currently, the deposit interest rate is at its highest in 14 years, as the ECB combats high inflation in the euro area, which reached 6.9% in Q1 2023. This represented a 25% decrease quarter on quarter.

Nevertheless, by comparing the separate components of inflation, it could be noticed that the food, alcohol & tobacco prices have risen by 11.6% QoQ, while energy prices decreased significantly by 104% QoQ, leading to deflation of that component. Consequently, we can conclude that such a decrease in inflation can mainly be attributed to decrease in energy prices, signaling the potential success of the ECB's actions in containing inflation (Eurostat, 2023).

SENTIMENT HITS RECORD LOW. A WIDENING GAP WITH SENTIMENT OUTLOOK.

The beginning of 2023 seems to continue the negative trend set in the first quarter of 2022, leading to a fifth consecutive decrease in the index from 4.3 in Q4 2022 to 4.1 in Q1 2023. This represents a decrease of 4.4% QoQ and 28.4% YoY. This result represents the lowest actual point recorded since the launch of the index in Q3 2019, and the second-lowest index value (average of actual and outlook). As we mentioned in our previous report, the current aggravated macroeconomic situation is severely impacting market perception among European investors, resulting in more pessimistic sentiment compared to the investors' perception on the previous distressed macroeconomic events from 2020.

Unlike in the previous quarter, investors waived their anticipations regarding the following quarter compared to the previous outlook for Q1 2023, with the outlook reaching 4.6 for Q2 2023, the same value as in Q3 2022, which represented the lowest outlook point recorded since the start of COVID-19 pandemic restrictions. The recorded 4.1 index actual differs significantly from the Q1 2023 outlook (measured in Q4 2022) which anticipated the index to reach a neutral point of 5.0. This negative effect could be explained by the banking crisis that was not expected to occur in Q4 2022 and significantly undermined European ventures.

Furthermore, it appears that increasing deposit interest rates might have triggered the banking crisis, has also managed to derail European attempts in reviving PE and VC markets. This has made it

difficult for both institutional and most private investors to allocate sufficient funds. We expect the European Central Bank to hold off with the new deposit interest rate changes since there is an urge to stabilize the banking situation in the region, which could probably be possible by either maintaining the current rate or lowering it with the potential threat of a return of high inflation. Therefore, the European VC market could be relieved with a lower or, at least, the same deposit interest rate.

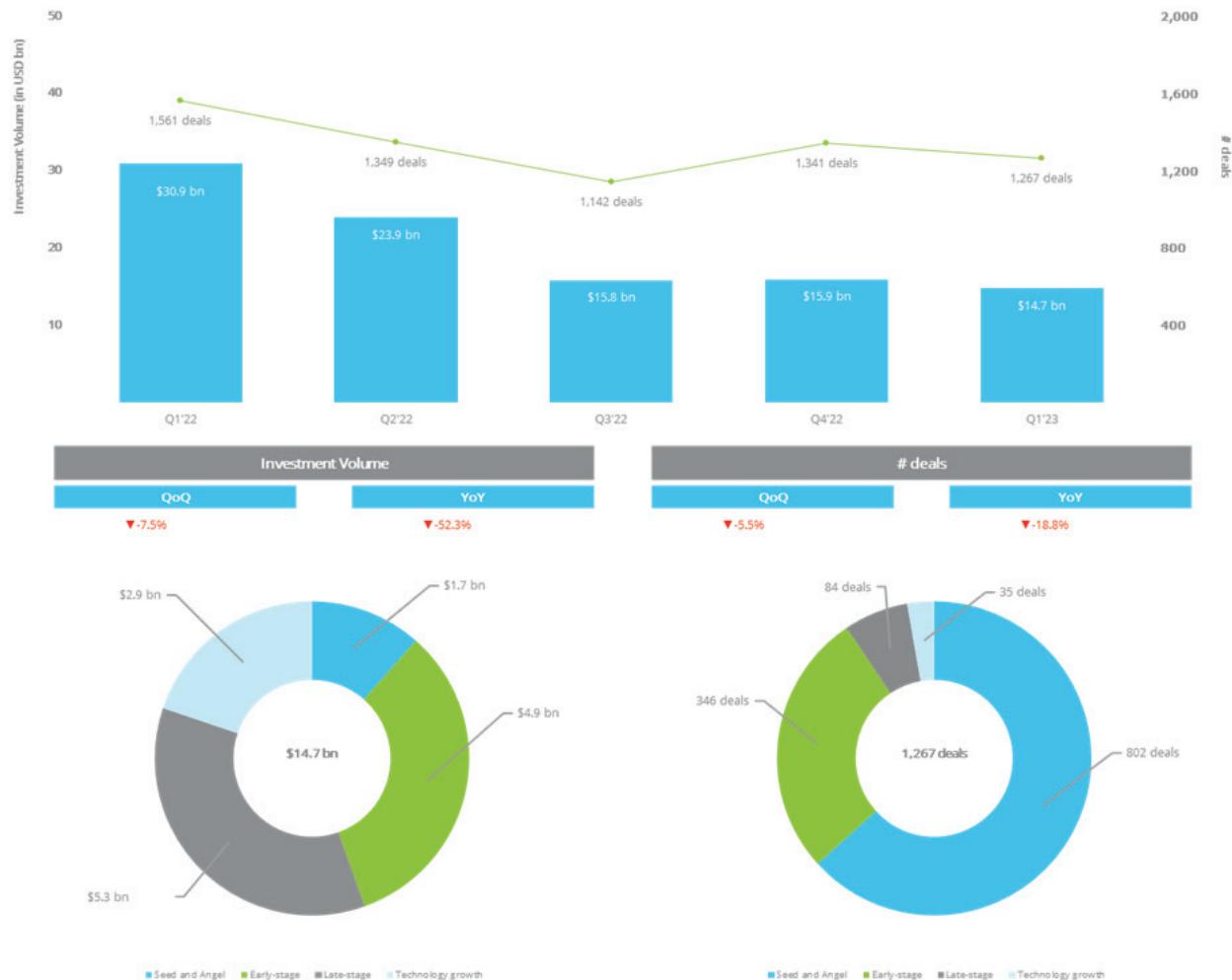
The most significant reductions in the index actual come from a 15.4% decrease QoQ in the perception of the current fundraising environment, and a 5.2% QoQ decrease in the sentiment about current state of startups' valuations. Additionally, respondents indicated a slightly lower sentiment for deal flow quality, deal competition, and the overall activity of European investors compared to Q4 2022. As a result, this is the first quarter where all components of the index experienced negative changes. The negative results in sentiment are also reflected in the European VC market, expressed in the decrease of overall investment volume, the total number of deals as well as average deal size.

The Q2 2023 outlook measured this quarter has decreased by 8.6% QoQ. The result is mainly driven by a 19.0% decrease in the anticipation of the overall activity of European investors combined with a decrease of 15.3% in the expectations regarding fundraising environment. The outlook for startups' valuations and the dealflow quality in the second quarter of 2023 are also negative. Participants indicated a positive outlook on deal competition levels which increased by 6.6% QoQ. At the moment, investors are primarily concerned with the interest rate policy of Central Banks, followed by the threat of continuing high inflation, the banking crisis, and the war in Ukraine.

Although the current quarter's actual results have been the most lacklustre since the inception of the index, and the outlook for the following quarter is below the neutral line, we anticipate that forthcoming quarters may show improvements due to the need for the ECB to defer deposit interest rate increases. This, in turn, may lead to a modest increase in venture investment activity and volume.

It is important to note, however, that the ECB has already acted in an unexpected manner by increasing the deposit rate during the banking crisis, so the opposite outcome could also be possible. Nevertheless, the aforementioned factors could potentially contribute to a more favourable economic climate in subsequent quarters.

EUROPEAN VENTURE CAPITAL DASHBOARD



OVERALL DECLINE IN VENTURE ACTIVITY.

In the first quarter of 2023, European venture capital investment experienced another slowdown, raising a total of USD 14.7 billion through 1,267 deals. This represents a 7.5% decrease (QoQ) and a significant 52.3% decrease YoY. A similar trend can be noticed in the total number of deals, which decreased by 5.5% (QoQ) and 18.8% (YoY).

The average deal size in this quarter was USD 11.64 million, 2.1% lower than in Q4 2022 and 41.2% lower than Q1 2023. This indicates the real impact of aforementioned macroeconomic events on the European Venture Capital market.

LEADING ECOSYSTEMS IN EUROPE SEE INCREASES IN VC ACTIVITY AMID CRISIS.

Europe's three largest European VC ecosystems have increased their aggregate investment volume over the course of the first quarter of 2023. The United Kingdom stands ahead with USD 4.8 billion total investment volume, resulting in a 37% increase on a QoQ basis.

The second leading venture ecosystem during the given quarter was France, raising USD 2.5 billion, which is a 39% increase compared to the previous quarter. The third place was taken by Germany with USD 1.9 billion investment volume, which represents a 12% increase (QoQ).

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We observe a drastic turnaround in investment volume distribution since the three largest European VC hubs represented 62.6% of the total raised investment in Europe compared to 44% in the previous quarter, which indicates that smaller VC hubs were mostly affected by the complicated macroeconomic environment, while the larger ecosystems have managed to increase their investments. Such a finding can be explained by the fact that investors from larger venture ecosystems were able to cope with the crisis better compared to the investors from smaller ecosystems.

Notably, the renewable energy sector dominated the European VC market, as evidenced by the fact that the three largest VC deals in the first quarter of 2023 were in this sector. This trend aligns with our predictions and observations presented in the previous reports about the high potential of this sector. We highlight the three most notable deals over the course of the given quarter. The first and the largest VC deal in Europe was an undisclosed-series venture financing round of Abound, a British-based consumer lending platform, which raised USD 601 million in March 2023 as part of its strategic investment.

The second largest VC deal of this quarter was a EUR 553 million private equity investment round of a Dutch-based developer, manufacturer, and operator of solar energy facilities, PowerField Netherlands. The third noteworthy deal was a pre-IPO venture financing round of ABB E-Mobility, a Swiss-based EV charging technology solutions provider, which successfully raised USD 356 million in February 2023.

METHODOLOGY

Over 4000 highly experienced investors (business angels, (corporate) venture fund managers and family offices) from 8 European countries were invited to participate in January, February and March 2023 in the European Venture Sentiment Survey, conducted by Venionaire Capital. Venionaire Capital collects answers from a focus group in computer-assisted personal interviews and a much smaller control group to assess the indices based on a quarterly recurring survey.

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 specific 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 start-ups 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. Start-ups 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 start-up 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.

THE EUROPEAN INVESTOR SENTIMENT INDEX

The index is based on feedback from different economic regions, as well as start-up 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. Berthold started his career in the statistics department of the Austrian Central Bank (OeNB).

"We attach great importance to providing our investors with an actual overview of the current investment climate in the European start-up sector. After this index has proven to be an important tool for our clients - including start-ups as well as investors - we have decided to make the results available to the public for the first time during the COVID-19 pandemic in the first quarter of 2020. Our aim was to draw public attention to the threatening situation of innovative young companies in Europe", explains Berthold Baurek-Karlic.

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AUTHORS



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

He is also founder and secretary general of the Business Angel Institute (businessangelinstitute.org), board member of the European Super Angels Club (superangels.club), Homepl (homepl.com), Flovtec (flovtec.com), Unmanned Life (unmanned.life) and chairman of the supervisory board of Blockpit (blockpit.io). Furthermore, he is an expert partner of various accelerators and consultants of various venture funds, as well as external consultant in the EU programs Horizon2020 (today Horizon Europe) and Innovation Radar.

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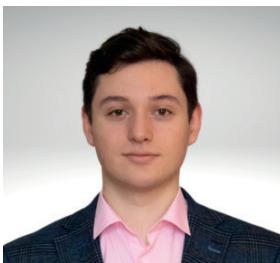
Victoria is a private equity expert with more than 10 years of experience in finance and private equity with an extensive international business network. She is leading deals and secondary transactions, supporting the setting up of new funds, and contributes her extensive operational expertise to our start-ups.



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Samuel manages deal flow, analyses business models and prepares investment decisions. Prior to Venionaire, Samuel has gained professional experience in London, Sofia, Vienna and Berlin.



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Denis supports our analysts regarding deal flow, analyses business models and prepares investment decisions. He has gained professional experience working on international projects between Russia and China. Denis is currently pursuing an undergraduate degree in International Business Administration with a finance major in Lauder Business School.

ABOUT



The European Venture Sentiment Survey is conducted with the lead of Venionaire Capital. Venionaire is a entrepreneurial partner for investors, founders and institutions. Our partners and team are specialized in venture capital and private equity investments, with an extensive over a decade-long track-record. We offer transaction and corporate advisory services – from due-diligence, valuation, deal structuring, (ghost) negotiating to alternative fund management – for investors, corporates, public entities and growth companies (startups / scaleups). Our track-record as entrepreneurs, advisors and investors shows deals in fields of corporate finance (M&A), (Corporate) venture capital, corporate startup engagement (CSE), digital transformation and high-tech innovation with a total volume of more than a billion Euros. In addition we serve as trusted partners for scouting, screening, technology-, market- and competitive analysis and valuation for bespoke investors and accelerators in Europe. We are proud of our performance within managed portfolios and increase our high-tech footprint everyday to support a future-proof economy.

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