

EUROPEAN INVESTOR SENTIMENT INDEX

Quarterly Survey

Q4/2023

January 15, 2024

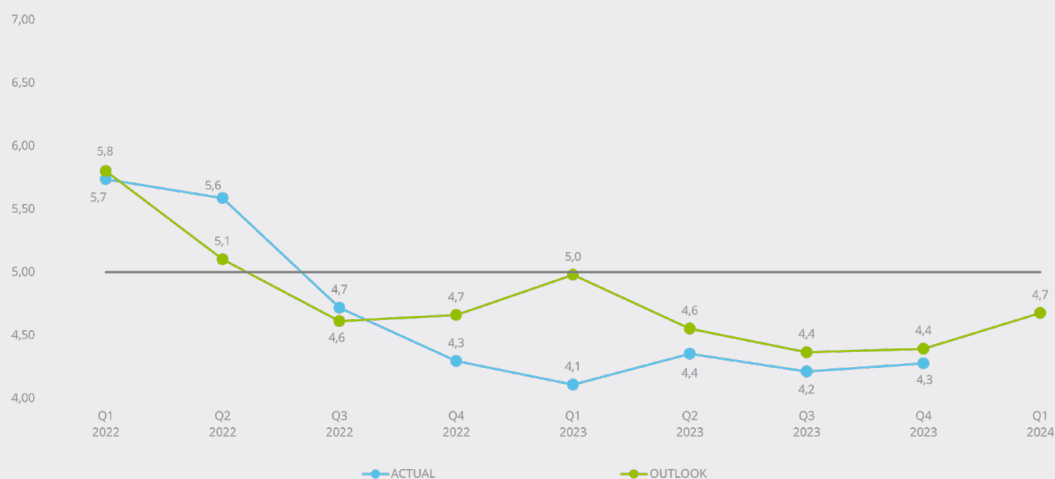
RESILIENCE AND RECOVERY OF EUROPEAN MARKETS AMID MACROECONOMIC CONCERNS.

The year has presented a multifaceted challenge for European investors, with several key factors impacting the region's venture capital (VC) market. Firstly, the persistent high inflation necessitated a shift in monetary policy, prompting Central Banks to engage in quantitative tightening. This shift played a pivotal role in precipitating a banking crisis, further complicating the investment landscape. Additionally, the ongoing military conflict in Ukraine has exerted a significant negative impact on the broader economic environment in the region. This has been particularly acute for European ventures and investors. Consequently, these combined factors have created a complex environment, posing substantial obstacles to the sustainable growth of the VC market in Europe.

Regarding the inflation levels, Euro area annual inflation has indicated a considerable deceleration by the end of 2023. The headline inflation rate in December 2023 stood at 2.9%, a substantial reduction from the high of 9.2 witnessed in December of the previous year. This decline is reflective of a notable easing in price pressures across various sectors of the economy. The main driver of that easing was the inflation of energy prices, which has registered a remarkable turnaround, transitioning from a steep 25.5% increase in December 2022 to a deflationary stance of -6.7% by December 2023. A significant reduction is also evident within food, alcohol, and tobacco. The composite inflation rate for this segment has declined to 6.1% from the previous year's 13.8%. This has built a ground to a decreased core inflation rate, which has dropped to 3.9% in December 2023 from 6.9% in December 2022 (Eurostat, 2024).

The notable reduction in inflation levels across Europe in 2023 can be largely attributed to the ECB's strategic tightening of its monetary policy. Throughout the year, the ECB implemented a series of measures, notably increasing the key interest rates six times in succession. The most recent hike occurred in September 2023, after which the ECB, aligning with market expectations, maintained its key rates steady: the main refinancing operations at 4.50%, the marginal lending facility at 4.75%, and the deposit facility at 4.00% (Euronews, 2023). This steadfast approach by the ECB was primarily aimed at curtailing the high inflation rates. With the gradual normalisation of inflation, as indicated by recent trends, it is anticipated that the ECB might halt further increases in key interest rates in the upcoming year. This expectation is based on the understanding that the primary objective of reducing inflation is being progressively achieved, thereby potentially easing the need for further rate hikes.

In 2023, the global financial sector was shaken by a banking crisis that included the collapse of Silicon Valley Bank (SVB) and significant turmoil within Credit Suisse. SVB, a key financier of technology startups, succumbed to a rapid withdrawal of deposits, compounded by losses on its bond portfolio due to rising interest rates. Its failure was the largest bank collapse since the 2008 financial crisis, sending shockwaves through not only the American VC community but also the European community, and prompting concerns about wider financial stability. Credit Suisse, on the other hand, grappled with a series of financial and reputational setbacks that eroded investor confidence. Despite efforts to restructure and address internal management issues, the bank faced liquidity concerns and saw its stock value plummet. These events underscored the vulnerabilities within the banking sector amidst a challenging economic environment characterized by tightening monetary policy, geopolitical tensions, and shifting market dynamics.



INDEX ACTUAL CONTINUES GRADUAL RECOVERY. OUTLOOK NEARS EXIT FROM NEGATIVE TERRITORY.

In accordance with the insights provided in our preceding quarterly report, it is evident that the European VC ecosystem is progressively moving towards recovery. This assertion is supported by the Q4 2023 index actual, exhibiting a marginal increase from 4.2 in Q3 2023 to 4.3 in Q4 2023, marking a QoQ rise of 1.6% and a minor YoY decrease of 0.4%. Notably, European investors have acknowledged the challenges faced by the ecosystem in 2023, anticipating a substantial reversal in the coming year amidst improving macroeconomic conditions.

This year, particularly in the fourth quarter, witnessed a notable shift in investor behaviour, with a pronounced inclination towards sustaining existing portfolio companies over exploring new opportunities. There was an observable trend of investors adopting a discerning approach ("cherry-picking"), and VC investors showed a preference for participation rather than leading funding rounds. Consequently, heightened complexities in securing necessary funding were further exacerbated due to a significant hurdle for startups in securing a lead investor in 2023.

The Q4 2023 index actual represents the third-lowest point recorded since its inception in Q3 2019, echoing a similar result from Q4 2022. The slight increase in the index actual for this quarter can be attributed to a moderate shift in investor concerns from macroeconomic conditions, which are gradually improving, to the heightened intricacies of fundraising for both funds and startups. Forward guidance for Q1 2024, with data recorded in this quarter, the index outlook stands at 4.7. This reflects a 6.4% increase compared to the previous quarter but signifies a 6.1% decrease compared to the previous year. The diminishing gap between the index outlook and the neutral line, coupled with the widening gap between the index actual for Q4 2023 and index outlook for Q1 2024, substantiates the trend identified in our two preceding reports. Investors anticipate improvements in the European VC ecosystem in the subsequent quarters of 2024.

The most notable increases in the index's actual values stem from a 12.0% QoQ surge in sentiment regarding deal competition, a 7.6% QoQ rise in sentiment regarding the current fundraising environment, a 6.3% improvement in investor activity, and a 4.1% increase in deal flow quality. Nevertheless, investors also indicated a 6.9% decrease in the current perception of startup valuations. Concerning the outlook for Q1 2024, respondents anticipate a 16.5% QoQ increase in the perceived valuation of startups, an 8.0% rise QoQ in deal flow quality, a 6.4% QoQ increase in future sentiment regarding deal competition, and a 5.0% QoQ rise in expectations for

the fundraising environment. Conversely, the index outlook includes a negative component — a 2.4% QoQ decrease in anticipated investor activity.

A predominant concern among investors remains the central banks' interest rates policy, followed by persistently moderate inflation, banking crises, and the conflict in Ukraine. Consequently, attracting LPs has become more complex for numerous investors, exacerbating startups' challenges in securing funding. Additionally, the unstable macroeconomic environment has compelled startups to pursue bridge rounds due to increased spending needs. Consistent with our earlier reports this year, we anticipate that, after navigating a complex landscape for both investors and startups, the European VC sector appears to be on a trajectory towards recovery in the coming year. However, it is crucial to underscore that such recovery may necessitate approximately 12-18 months before witnessing significant growth.



Amidst the persistently intricate macroeconomic landscape in Europe, we observed that the latter part of 2023 witnessed a notable upturn in VC activity within the European ecosystem, contrasting with the earlier part of the same year. A crucial shift within this landscape has been the distinctive reduction in the involvement of US-based VC investors in European funding rounds. Remarkably, this decline was concurrently accompanied by a substantial surge in investment volume during this quarter, surpassing figures from both the preceding quarter and the preceding year. This noteworthy shift is noticeable in both early-stage funding rounds, where American participation fell below the 20% mark, and late-stage funding rounds, where it dipped below 45%. Consequently, this trend underscores a pivotal development — despite the waning interest of American investors in European startups, the investment landscape in the region exhibits a gradual recovery, primarily attributed to the growing significance of local capital.

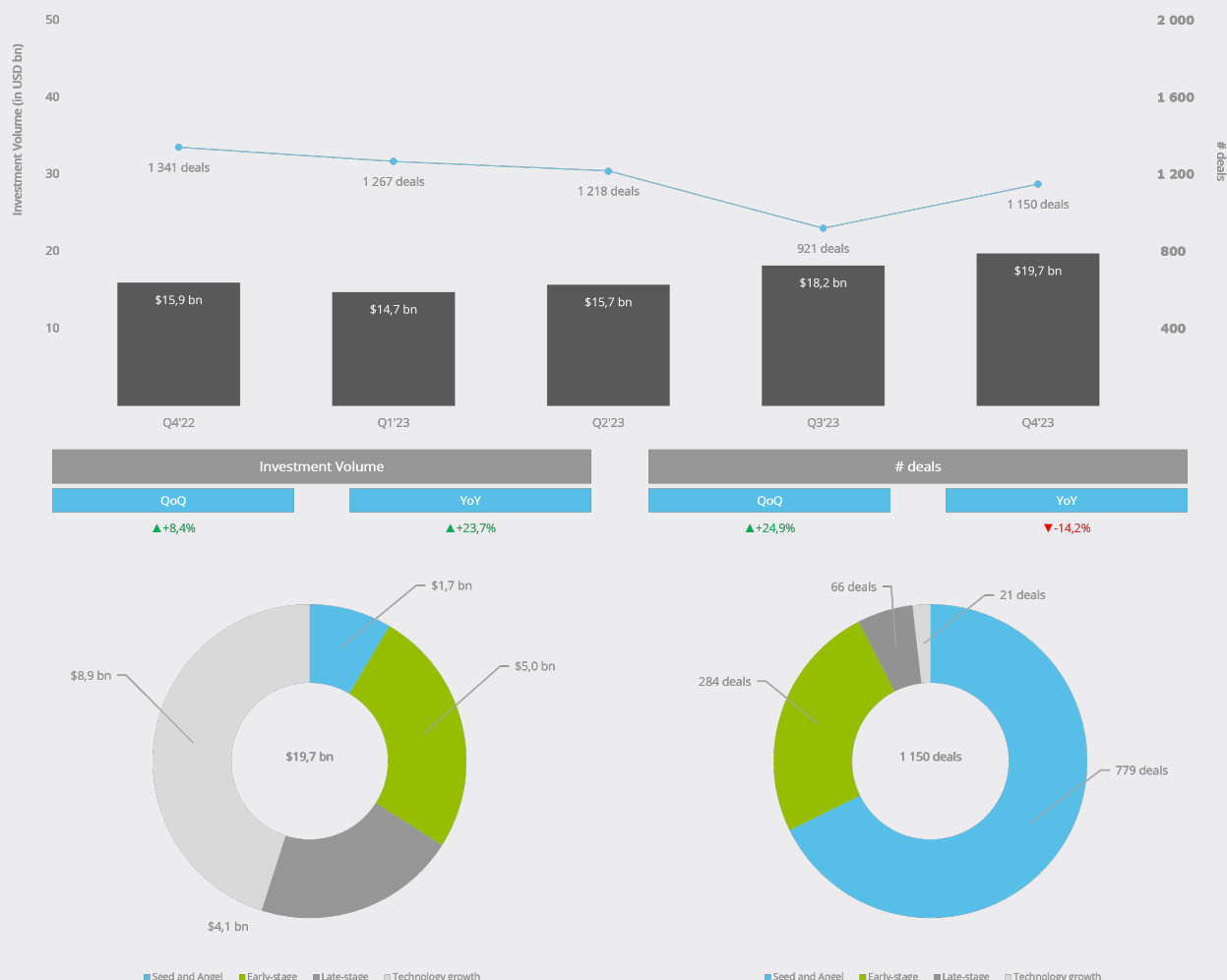
Furthermore, during our in-depth interviews with key European VC investors, a crucial observation came to the fore. Specifically, European median startups' valuations seem to normalise after turbulence experienced during this year. This transition is particularly evident as valuations across diverse funding stages appear to be reverting to their historical 5- and 10-year averages, with the exception of Seed round valuations, which continue to exceed their historical averages. We anticipate that valuations within this stage are likely to experience a correction and, as a result, close the gap with the 5- and 10-year averages, albeit this correction can be expected over a timeframe spanning from 6 to 12 months.

Berthold Baurek-Karlic
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EUROPEAN INVESTOR SENTIMENT INDEX Q4/2023



EUROPEAN VENTURE CAPITAL DASHBOARD



EUROPEAN VC SHOWS CONTINUING RECOVERY. YET STARTUPS ARE STRUGGLING WITH FUNDRAISING.

In the fourth quarter of 2023, European ventures secured a cumulative funding of USD 19.7b across 1,150 deals, marking a continuation of the sector's gradual recovery that began to emerge in the second quarter of 2023. This performance indicates an 8.4% increase in investment volume compared to the previous quarter and a significant 23.7% compared to the previous year. Notably, this quarter is the first since Q4 2022 to register an uptick in deal count,

with a substantial 24.9% rise from the previous quarter, albeit a 14.2% decline from the previous year.

The average deal size in Q4 2023 stood at USD 17.1m, down 13.1% from USD 19.7m in the preceding quarter but up a remarkable 44.2% from USD 11.9m in the same period last year. Despite a slight reduction in average deal size this quarter, the trend underscores investors' heightened caution and stringent investment criteria, focusing primarily on portfolio startups. Consequently, the increase in deal numbers has not outpaced the gradual recovery in investment volume across Europe, placing considerable strain on startups that last raised funds in early to mid-2022. These companies are now compelled to seek additional funding amidst challenging fundraising conditions.

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Insights from personal interviews with European VC investors reveal a noticeable contraction in the available funding pool, intensifying competition for startup capital. This environment has led to European VCs increasingly specializing in specific industries. Another key observation is the heightened rigor in initial due diligence, with investors demanding more comprehensive information upfront.

Moreover, many investors pointed to significantly constrained exit opportunities for mature startups, primarily attributable to ongoing macroeconomic challenges, though these appear to be easing gradually. Nonetheless, exit strategies remain a critical concern for mature startups, with many attempting to improve exit conditions. This situation has led to delays and the need for additional funding rounds. As a result, European ventures recorded a total of 848 exits in this quarter (835 from M&A, 10 from IPOs, and 3 from SPACs), representing a 9.3% quarter-over-quarter increase but a 7.4% decline compared to the previous year.

FRANCE CLOSES GAP ON THE UK, WHILE GERMANY LAGS BEHIND.

In the final quarter of 2023, the United Kingdom, France, and Germany emerged as the three most prominent VC ecosystems in Europe. Collectively, these top three ecosystems accounted for a striking 78.3% of the total investment volume in Europe during this period, reflecting a notable 14.8% increase from the previous quarter. The UK and France both experienced growth in their investment volumes, while Germany witnessed a slight decline compared to its performance in the preceding quarter.

Leading the way, the United Kingdom, Europe's largest VC ecosystem, attracted a total investment of USD 7.1b, a modest 3.1% increase from the previous quarter. France, holding the second position, saw a remarkable 81.9% quarter-over-quarter surge in investment volume, closing the gap to the UK significantly, with a total investment of USD 6.8b. In contrast, Germany's VC ecosystem experienced a slight downturn, with a 6.8% decrease in total investment volume, amounting to USD 1.6b.

The quarter was marked by three significant funding rounds within the European VC landscape. The largest transaction was a Series B funding round for a German-based AI technology startup, which secured USD 500m in November 2023. The second largest deal involved Mistral AI, a French open-source platform developer that assembles team to develop AI models, which completed a USD 415m Series A funding round in December 2023. The third notable transaction was a Series F funding round for SumUp, a UK-based FinTech firm specializing in card payment solutions for businesses, both at POS and on the go. This round, finalized in December 2023, raised USD 307m (Dealmatrix, 2024; Crunchbase, 2024).

METHODOLOGY

Over 4000 highly experienced investors (business angels, (corporate) venture fund managers and family offices) from 8 European countries were invited to participate in October, November and December 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.

REFERENCES

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AUTHORS



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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 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), Homeppl (homeppl.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.



DENIS VOLDMAN
ANALYST, VENIONAIRE CAPITAL

Denis manages the dealflow, analyses intricate business models, and prepares investment decisions. He is accountable for spotting, screening, and evaluating startups, with an added focus on financial modelling, aiding Venionaire's clients with financial engineering and valuations. Additionally, Denis is responsible for evaluating the development of portfolio startups. He has gained professional experience working on international projects between Russia and China. Holding an undergraduate degree in International Business Administration with a finance major from Lauder Business School, he currently pursues a graduate degree in Strategic Finance & Business Analytics from the same institution.



SOFIYA LYN
ANALYST, VENIONAIRE CAPITAL

Sofiya is responsible for the preparation of information for reports and manages various dealflow tasks, which encompass fundraising efforts and the ongoing updating of startup information. She is also actively involved in assisting with the identification, evaluation, and consideration of potential startups. Sofiya earned her Bachelor of Arts degree in the "Ethics Politics Economics" program from the Ukrainian Catholic University in Lviv, Ukraine, achieving the distinction of magna cum laude. Currently, she is pursuing her Master of Arts degree in Economic Policy in Global Markets at the Central European University. Additionally, she possesses valuable experience in international cooperation, garnered during her tenure at the Economic Department of the Ukrainian Embassy in Austria.

ABOUT



The European Venture Sentiment Survey is conducted with the lead of Venionaire Capital. Venionaire is a entrepreneurial partner for investors, founders and institutionals. 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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