KPMG

US Venture Capital Valuation Trends Report 2021

March 2022

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Introduction

Welcome to this special report on US Venture Capital (VC) valuations which explores some of the highlights of venture capital in 2021 and the drivers behind valuation movements in the year. Asset managers in venture capital have the opportunity to drive value through their expertise, industry connections, and long-term investment horizon. Through December 31, 2020, Cambridge Associate's US Venture Capital benchmark annualized return over the past 25 years was 32.4% and greatly outperformed the NASDAQ(11.3%), Russell 2000(9.1%), and S&P 500(9.6%)[(1)] over that period. This trend of outperformance has continued into 2021.

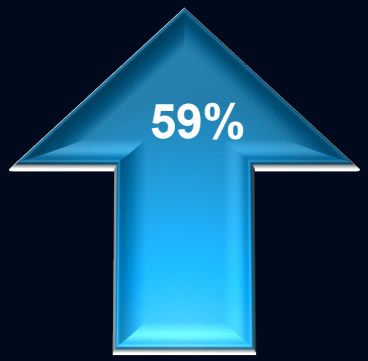
Late-Stage VC-backed enterprise tech companies saw their median pre-money valuations jump to $150M from $70M in 2020[(2)]. Also late-stage fintech companies had standout results with their median pre-money valuations jumping to $272M in 2021 compared to $151M in 2020[(2)]. In a year where there were a record number and record valuations for VC-backed companies exiting, these valuation lifts in the private space are staying on trend.

We see many asset managers benefiting from the surge in valuations and favorable fundraising environment. The key drivers of these private VC valuations in our view are increased competition, increasing allocations to US VC overall and dry powder, and US VC's historical track record of over-performance relative to other asset classes. Looking at supply and demand we can gain insights into the dynamics of driving market forces in the determination of portfolio company valuations.

Introduction (continued)

What happened to valuations and capital raising in 2021 for US VC?

Increase in average Pre-Money Valuations in 2021 for late-stage companies*



Increase in Exit Step-up multiples for VC-backed public listing valuations in 2021*

61.8%

The percentage of capital raised by North American VC firms as a percentage of Global VC capital raised in 2021*

$443.8B

The amount of Global Venture Capital Dry Powder as of March 31, 2021 – a record amount*

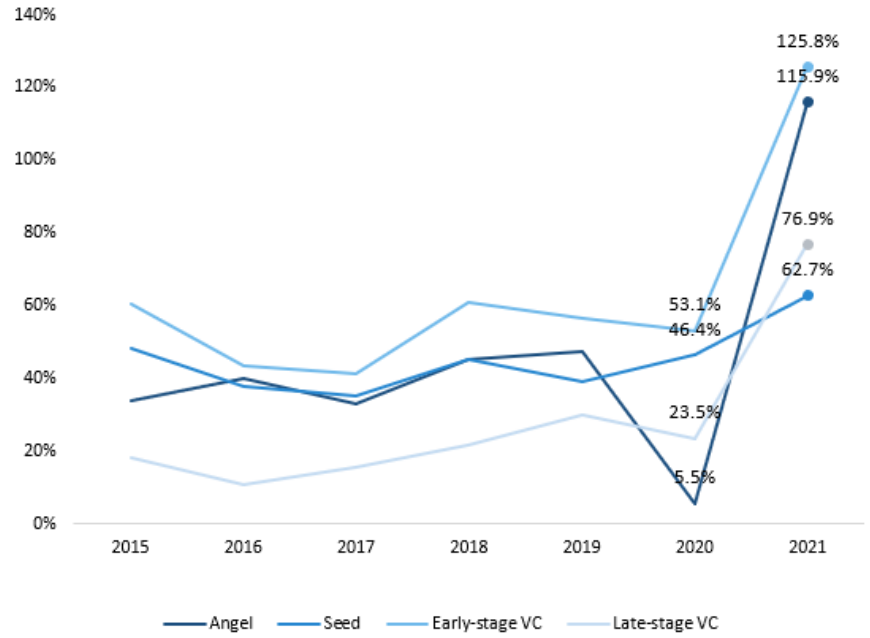
*Source: PitchBook Data, Inc.

US Venture Capital
2021 Valuation Movements

One of the most telling statistics for just how much US VC valuations moved in 2021 can be seen by the rate of increase in valuations between private financing rounds. The relative velocity of value creation (RVVC) or annualized percentage increase in valuation between financing rounds, has grown across most stages of the portfolio company lifecycle. Looking at this metric from Pre-COVID 2019 and comparing to 2021, the changes are significant.

As we can see in the graph to the right, Median RVVC has increased on average from 42.6% in 2019, dipping to 31.5% in 2020 and increasing to 72.9% for the year-ended December 31, 2021. Effectively, the annualized median rate of valuation increases between financing rounds has increased by 231% in 2021 relative to 2020. This hasn't occurred since 2010 at the beginning of the recovery from the Financial Crisis.

Median relative velocity of value creation

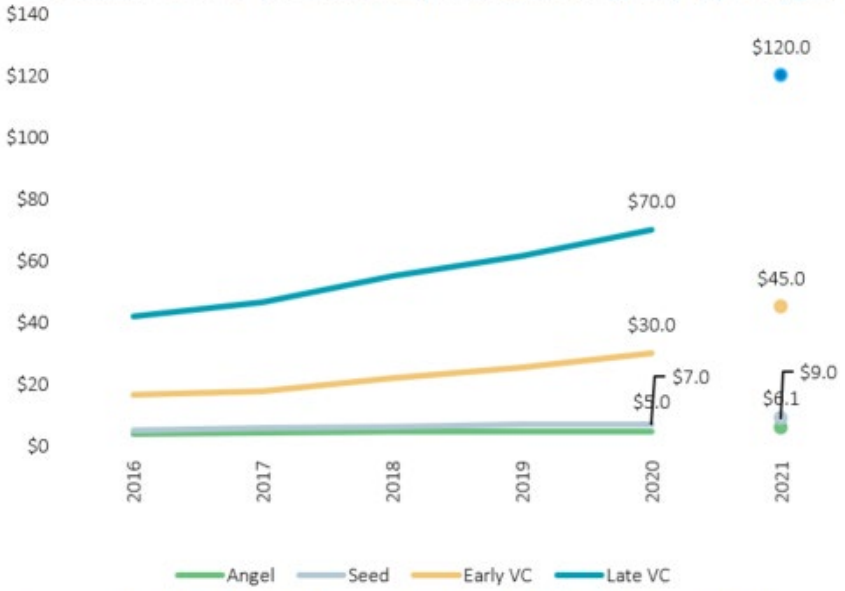


Source: PitchBook Data, Inc. - Q4 2021 Annual US VC Valuations Report

2021 Valuation Movements (continued)

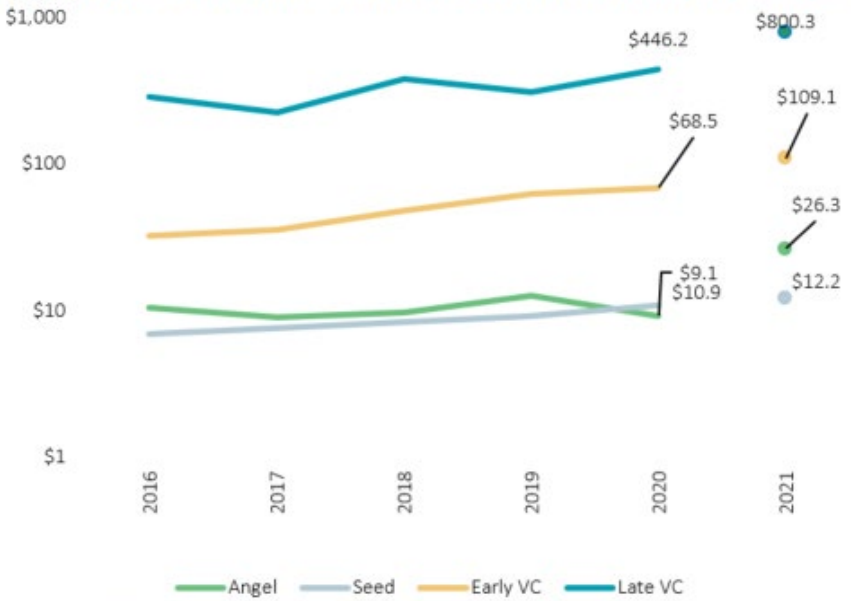
The median and average US VC pre-money portfolio company valuations have increased drastically. In particular the average pre-money valuation for US late-stage VC has increased 260% to $800.3M in 2021 relative to $307M in 2019. This outpaces all other categories of venture stages with angel-stage increasing 209%, seed-stage increasing 134%, and early-stage increasing 174% in average pre-money valuations over the same period.

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



Source: PitchBook Data, Inc. - PitchBook-NVCA Venture Monitor Q3 2021

Average US VC pre-money valuation ($M) by stage

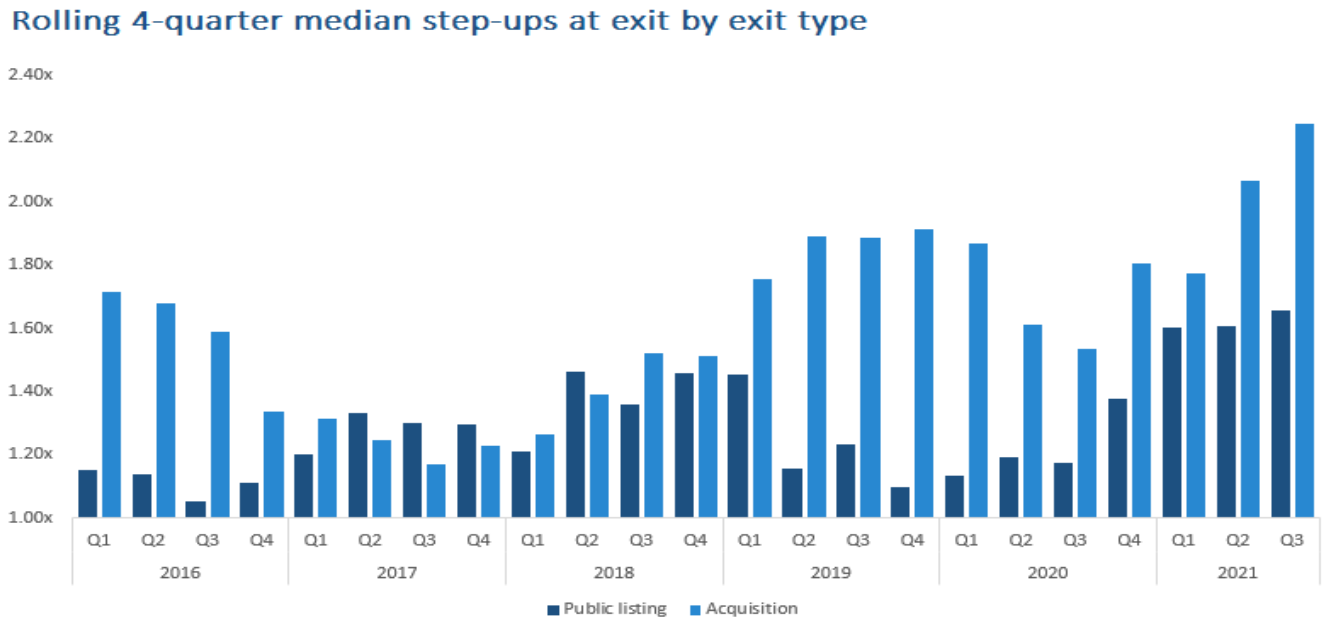


Source: PitchBook Data, Inc. - PitchBook-NVCA Venture Monitor Q3 2021

2021 Valuation Movements (continued)

On the exit side, a similar valuation story continues with exit valuations relative to previous private financing round valuations (i.e. step-up valuations) at stand out levels. Even with increasing private valuations, exit valuation step-ups are at their highest points in the last five years.

Exit values for portfolio companies show a clear benefit on exits via acquisitions as opposed to public listing valuation step-ups, although both have shown large increases in 2021. As of September 30, 2021, the rolling 4-quarter median exit step-up was 2.25X on acquisitions, increased from 1.81X as of December 31, 2020. Public listings as of September 30, 2021 increased to a rolling 4-quarter step-up multiple of 1.66X from 1.38X as of December 31, 2020. This data suggests there is an increased willingness to increase price when it comes to corporates with strategic benefits from the purchase. Part of this could be driven by the increasing liquidity where there is $2.6T in US Nonfinancial corporate currency and deposits as of September 30, 2021[3]. This is an increase from $1.9T as of December 31, 2019.



Source: PitchBook Data, Inc. - Q3 2021 Annual US VC Valuations Report

US Venture Capital
Demand Factors

The competitiveness of asset managers and capital allocated to US VC are going to be significant drivers of demand. In turn these factors will impact economic and non-economic negotiations with portfolio companies. All else equal, an increased number and size of US VC investment funds will organically drive competition and valuation increases. Also, the composition of investors can also drive demand, particularly in the case of corporate venture funds which may have strategic, in addition to direct financial considerations.

Capital allocations

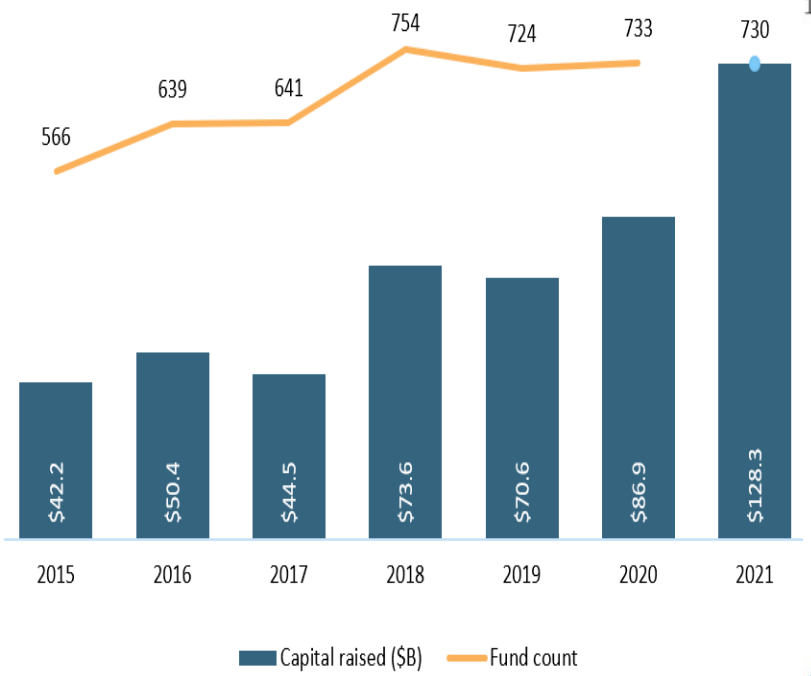
With the Fed funds rate in the US rising in 2022, increased quantitative easing and rising inflation, it's key for asset managers to be able to maximize their real rates of return. Alternative investment strategies, and in particular venture capital is increasingly attractive as a result of its ability to generate alpha.

According to a recent McKinsey article, the number of US listed public companies has decreased from 5,500 in 2000 to about 4,000 in 2020[(4)]. This makes allocations to private capital strategies more attractive given there are fewer public companies in the US in which to invest. According to PitchBook-NVCA's Q4 2021 Venture Monitor Report, through December 31, 2021, fundraising for US VC hit a record $128B in capital raised on 730 funds, which is an 82% increase from 2019 which saw $70.6B in capital raised on 724 funds. Furthermore, North American VC has been taking an increasingly larger portion of global VC capital raised with an increase to 61.8% in 2021 from 37.2% in 2019. This influx in capital generates tailwinds towards demand for portfolio companies and competition in the fundraising process.

Demand Factors (continued)

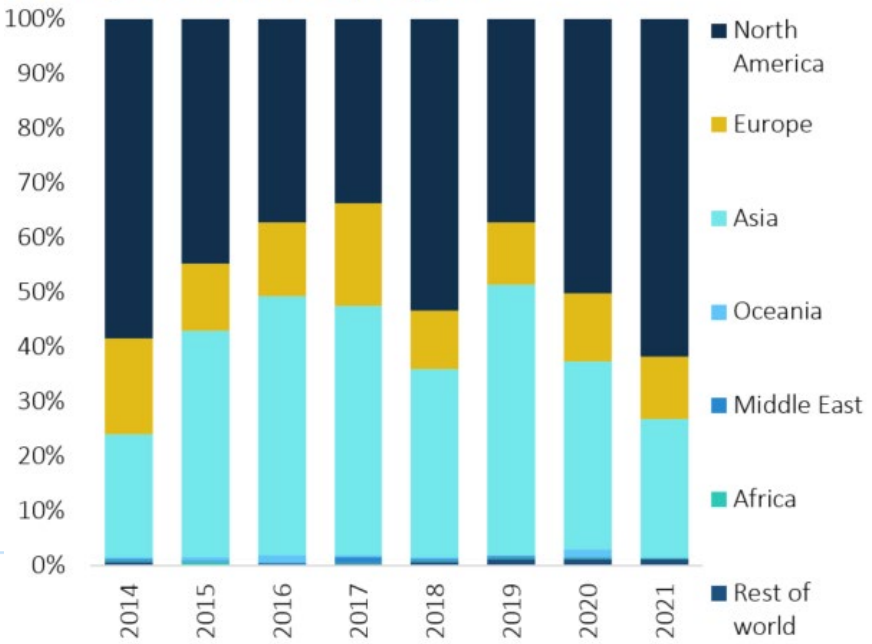
US VC fundraising hits all time high and North American VC as a percentage of global VC capital raised increases to 61.8%

US VC fundraising activity



Source: PitchBook Data, Inc. - PitchBook - NVCA Venture Monitor Q4 2021

VC capital raised by region

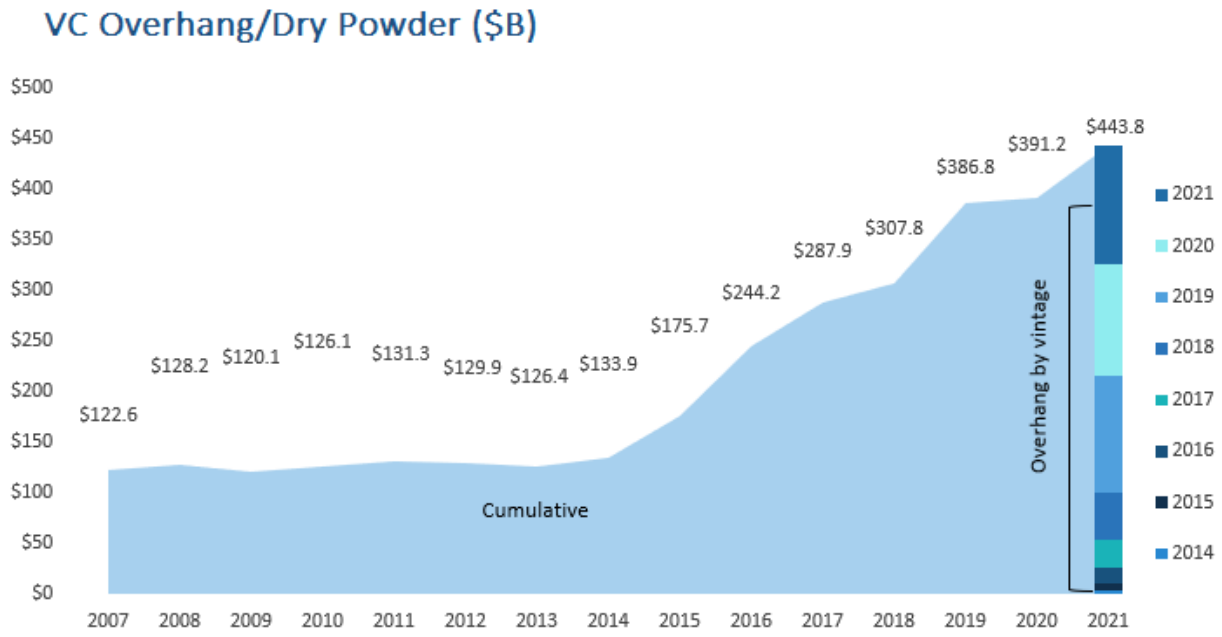


Source: PitchBook Data, Inc. - Q3 2021 Private Fund Strategies Report

Demand Factors (continued)

VC Dry Powder

Another tailwind for deal competition and fundraising is indicated by dry powder (or VC overhang) held in venture capital funds. This is the amount of capital commitments a fund has on its hands but is uninvested by the fund. Globally, the dry powder in VC funds has reached a record of $443.8B. Dry powder is comprised mostly of funds launched in the previous three years which is dominated by North American funds and in turn US asset managers needing to invest capital in 2021 to meet their investment period mandates. This increase in capital available for investment will drive increased competition and portfolio company valuations.



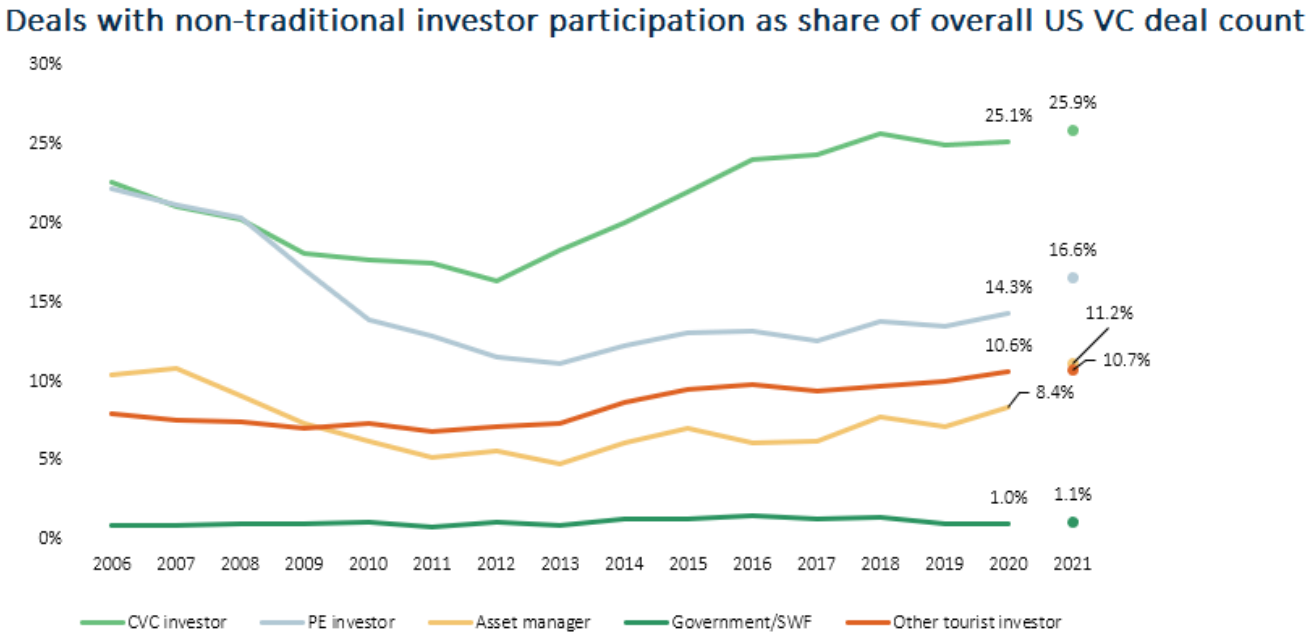
Source: PitchBook Data, Inc. - PitchBook Private Fund Strategies Report Summary Q3 2021 (As of March 31, 2021)

Demand Factors (continued)

Market participant composition

Interest in US VC is not just from pure-play venture funds. Also increasingly involved in the space are cross-over funds, sovereign wealth funds, corporate venture funds, amongst other non-traditional VC investors. Some hedge funds will allocate a portion of their capital into the private space consistent with their core strategy and to help earn asymmetric returns.

Furthermore, corporate venture funds see an opportunity to obtain financial returns but also synergies from alliances with portfolio companies in their industry and potentially value-added through acquisitions. With low borrowing rates and significant levels of corporate cash, it's an attractive time to fund acquisitions, or investments into fund structures with a corporate-aligned VC mandate. In 2021 there was an increase across five main categories of non-traditional venture capital investors. Overall as indicated in the below graph, involvement by non-traditional investors based on deal count has increased from 56.6% in 2019 to 65.5% on September 30, 2021.

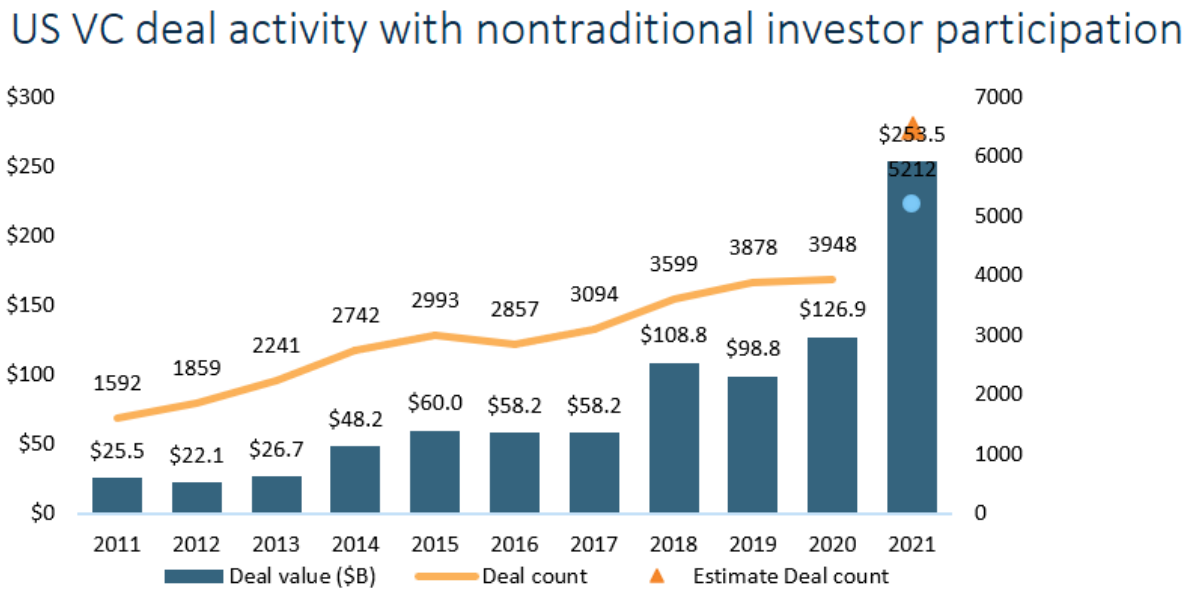


Source: PitchBook Data, Inc. - PitchBook-NVCA Venture Monitor Q3 2021

Demand Factors (continued)

Market participant composition (continued)

Involvement of non-traditional investors such as sovereign wealth funds, private equity growth funds, hedge funds, and corporate venture funds have grown from $98.8B in 2019 across 3,878 deals to $253.5B and 5,212 deals through December 31, 2021. According to PitchBook-NVCA's Q3 2021 Venture Monitor Report, as of September 30, 2021, non-traditional investor deal value in late-stage companies amounted to $146B, which is a 99% increase compared to $73B in deal value in 2019 by this investor group. This outpaces overall growth in deal value over that time which was 67%. This suggests the impact from non-traditional investors is felt in late stage portfolio company valuations, where the companies are more mature and exit timing is more visible.



Source: PitchBook Data, Inc. - PitchBook-NVCA Venture Monitor Q4 2021

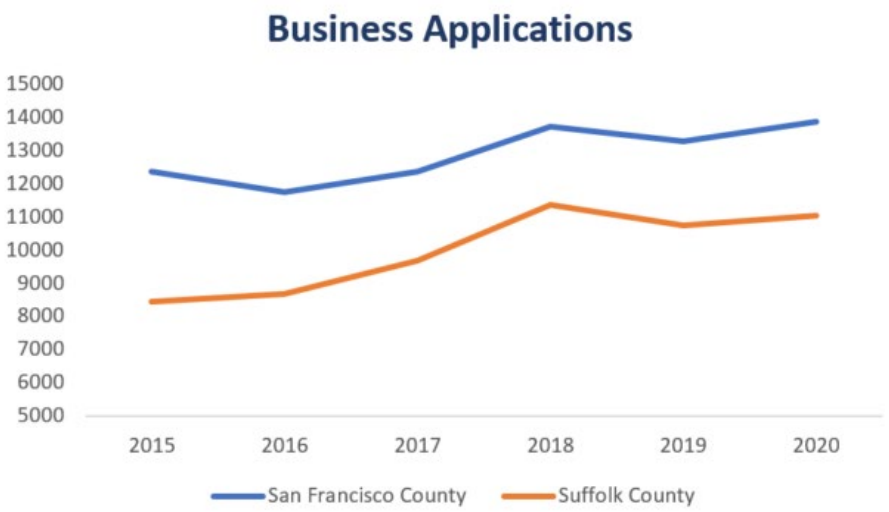
US Venture Capital
Supply Factors

The number of private companies, private company formations and bankruptcies will directly impact the investment opportunity set available to asset managers, and competition for fundraising. The data shown here suggests that the rate of increase in private company formations has not maintained pace with capital raised in US VC.

Business formation statistics

US Real GDP grew 5.7% year over year in 2021 compared to 2020[5]. The combination of economic growth with a low US federal funds rate has created an environment which is friendly for new company formations and economic growth.

We can see the number of business applications in the San Francisco and Boston area, two strongholds for venture capital, have been relatively stable since 2018 but have been increasing since 2016. This gives insight that there is potentially an increasing number of companies seeking venture-back financing but at a lower rate than capital flows and growth in VC dry powder.

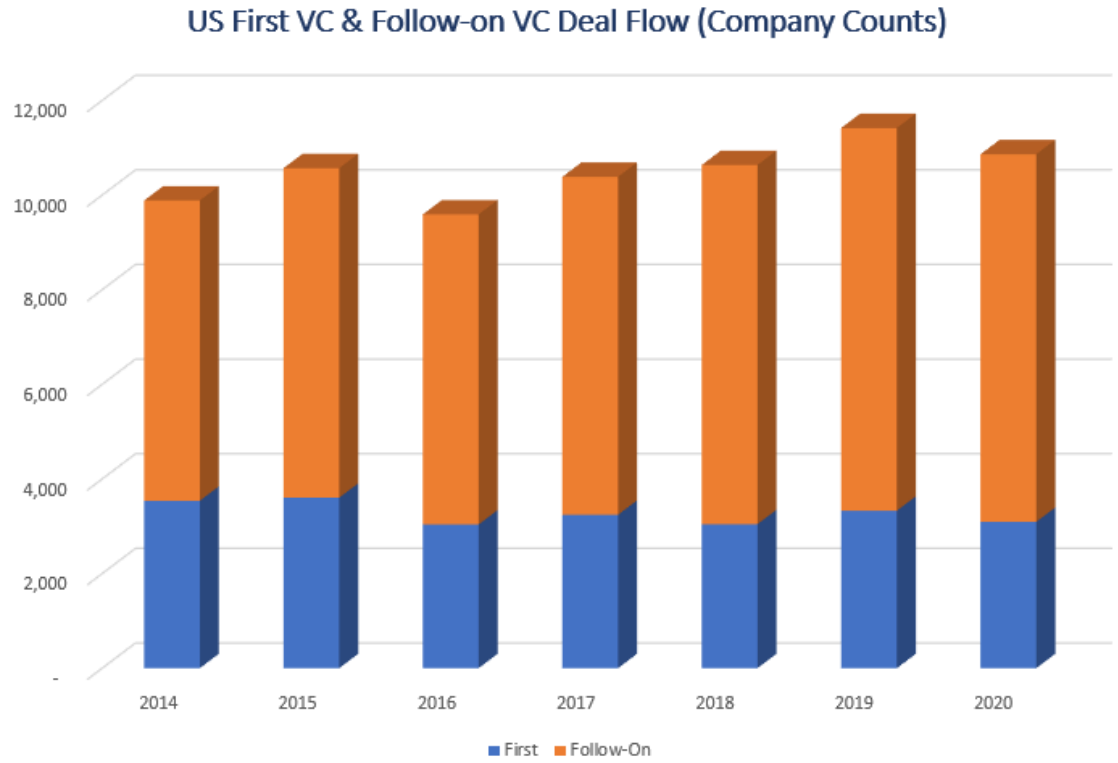


Source: United States Census Bureau

Supply factors (continued)

Venture capital portfolio company count

The proportion of portfolio companies receiving venture financing for the first time versus follow-up financing has stayed relatively consistent over the past six years and has been growing gradually. With the growing number of companies receiving venture capital financing, and reduced bankruptcy filings from 2020 to 2021[6], this indicates increased supply putting downward pressure on valuations. Compared to capital inflows which grew 47% year over year, the increase in venture-backed companies hasn't kept the same pace and points to part of the reason why valuation rises are more demand driven.

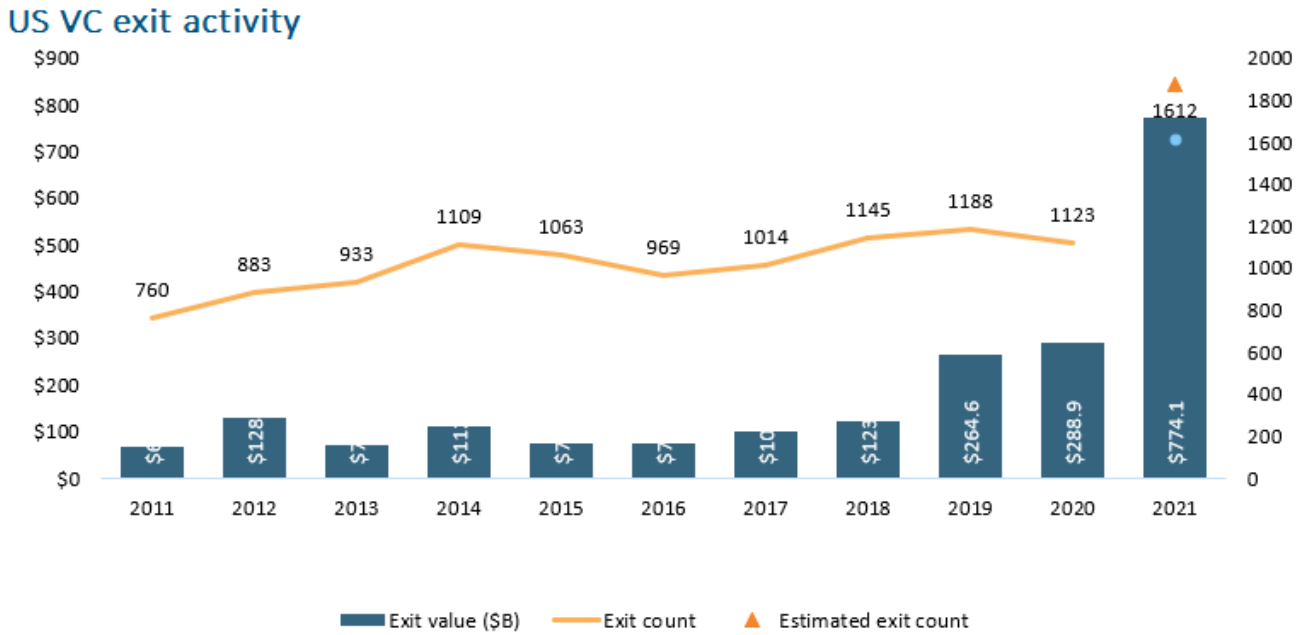


Source: NVCA 2021 Yearbook, data provided by PitchBook Data, Inc.

Supply factors (continued)

US VC Exit Activity

The level of IPO and M&A activity for venture-backed companies year over year has changed meaningfully and likely has been a driver in the change of valuations for VC-backed companies fundraising. US VC exit activity in 2021 shows that the number of US VC portfolio company exits were 1,612, or a 43% increase in exits over the 1,123 exits seen in 2020. According to PitchBook-NVCA's Q4 2021 Venture Monitor Report, there was an increase in US SPAC activity which went from 230 deals in 2020 to 556 deals in 2021, and this appears to be a large driver of the exit activity in 2021. This would be another tailwind for remaining private companies looking at fundraising with an increased number of counterparts being acquired or going public and thus limiting competition for financing. The increased number of exits and attractive step-up valuations at exit provide a basis for later-stage investors to validate higher valuations for their portfolio companies.



Source: Pitchbook Data, Inc. - PitchBook-NVCA Venture Monitor Summary Q4 2021

US Venture Capital

Final Thoughts

US Venture Capital fundraising in 2021 reached all-time highs. Along with this trend, there has been a build up of dry powder and capital available for investment in 2021. There is increased diversification of investors allocating to venture capital in 2021 as well, particularly in late-stage companies. These have been dominant factors in driving US Venture Capital valuations to all-time highs. The increased volume of portfolio company exits and increasing exit valuations since 2017 are attractive liquidity outcomes for the industry as a whole and capital allocators.

From 2018 through 2020, the number of business applications in the US have been relatively stable, and we can see in key venture hubs such as the Bay Area and Boston, the situation is largely the same. Likewise, over the same period the number of companies obtaining venture financing have been relatively flat in comparison to fluctuations in capital allocations into US VC.

Given these trends, there is a clear signal that valuation movements are being demand driven. Although not seen yet, in the medium to longer term, potential headwinds could result from reduced VC fundraising and dry powder in US VC driven by tighter monetary policy. Also headwinds to valuation could occur through a reversion towards Non-US VC firms like was seen in 2015 through 2017. If there's a continued pull-back in public market valuations, particularly in the technology space, this also could lead to a retreat in private market valuations as the prospect on exit valuations will be decreased.

The Russia-Ukraine conflict will certainly impact global venture capital. Due to greater geopolitical risk, we could see reduced valuations if there is European operational exposure for a portfolio company. We could see overallocation of capital to the US with a view as a safer alternative during this conflict. The downstream impact would then be more demand for US-centric private companies and increased valuations there.

The RVVC between financing rounds in 2021 are at levels that we have not seen since the recovery from the Financial Crisis, and this indicates a bounce-back from 2020 COVID-19 market impacts. Overall based on historical RVVC trends, we could expect to continue seeing increasing valuations in 2022 with a pull-back on the rate of valuation increases over the near-term.

References

1 https://www.cambridgeassociates.com/benchmarks/us-pe-vc-benchmark-commentary-calendar-year-2020/

2 Source: PitchBook Data, Inc. - PitchBook 2021 Annual US VC Valuation report

3 Economic Research - Federal Reserve Bank of St. Louis

4 https://www.mckinsey.com/business-functions/strategy-and-corporate-finance/our-insights/reports-of-corporates-demise-have-been-greatly-exaggerated

5 https://www.bea.gov/news/2022/gross-domestic-product-fourth-quarter-and-year-2021-advance-estimate#:~:text=Real%20GDP%20increased%205.7%20percent,in%202020%20(table%201)

6 https://finance.yahoo.com/news/overall-december-2021-bankruptcy-filings-171200444.html

Data Source

PitchBook has been used as the provider of venture data used in this report. Other sources where applicable have been noted. Below are definitions for terms used throughout this report.

Angel/Seed-stage: PitchBook defines financings as angel rounds if there are no PE or VC firms involved in the company to date and it cannot be determined if any private equity or venture capital firms are participating. In addition, if there is a press release that states the round is an angel round, 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. When the investors and/or press release state that a round is a seed financing, or it is for less than $500,000 and is the first round as reported by a government filing, it is classified as such. If angels are the only investors, then a round is only marked as seed if it is explicitly stated.

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 or later (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.

Corporate venture capital: Financings classified as corporate venture capital include rounds that saw both firms investing via established CVC arms or corporations making equity investments off balance sheets or whatever other non-CVC method is employed.

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.

Exits: PitchBook includes 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 PitchBook track’s 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: PitchBook define’s 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 private equity 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 headquarters 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

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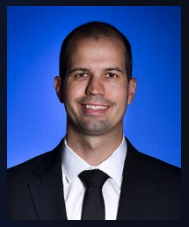

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