Trends in Venture Capital

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The trends

- Returns have been poor over the past decade
- The industry has begun to shrink
- Investment activity has plateaued
- VC funds are slowly reverting to their earlier form
LP’s haven’t been making money

Source: Created from data collected by Cambridge Associates, LLC
Portfolio company age at IPO is increasing

Source: Created from data collected by Professor Jay Ritter, University of Florida
The IPO market has shrunk

- VC-backed IPOs have been scarce since 2000
- IPOs as a percentage of companies financed five years earlier fell to a paltry 0.3 percent in 2009 from 25 percent in the 1990s
- In 2008 and 2009, the ratio of VC-backed M&As to IPOs was 47.5, a far cry from 2.0 for the 1992 to 1999 period.
- The real dollar value of the average IPO deal dropped from $90.9 million in 2007 to $58 million in 2009
- But the VC-backed share of IPOs was essentially the same from 2001-2009 as it was from 1990-1998 (36% versus 34%)
VC-Backed IPOs down substantially since 2000

Source: Created from data collected by Professor Jay Ritter, University of Florida
IPOs as percent of VC investments five years prior have fallen more

Source: Created from data collected by the National Venture Capital Association (NVCA)
Value of companies at IPO is declining

Source: Created from data from Dow Jones Venture Source
VC-backed M&A market is stagnant

• In 2009, VC-backed M&As were 11 percent of companies financed five years earlier, down from 30 percent in the 1990s
• The average real dollar amount of money raised per VC-backed M&A deal dropped from $114.6 million in 2007 to $43.3 million in 2009
Exits through M&A began to decline in the mid-2000s

Source: Created from data in Dow Jones Venture Source
Decline in M&As as percent of investments five years prior

Source: Created from data collected by the NVCA and Dow Jones Venture Source
Value of companies at M&A hit by financial crisis

Source: Created from data from Dow Jones Venture Source
Investment outcomes are affecting the industry

• Low LP returns from venture capital investments leading them to reallocate capital away from VCs
• As poor VC returns have hit fundraising, capital under management has declined
• VCs have been exiting the industry
• Number of companies financed and dollars invested are stagnating
Numbers are back to mid-1990s levels

- Number of venture capital funds was down to 1,188 in 2009, the lowest number since 1999
- Only 127 funds were raising money, the lowest level since 1993
- Capital under management fell to $179 billion in 2009, the lowest level in real dollar terms since 1998
- VCs invested $18 billion in start-ups, the smallest amount in real terms since 1996
- VCs made 2,802 deals, investing in 2,372 companies, also the lowest number since 1996
- The 728 companies that received first-time and the $3.3 billion in first-time financing were the lowest since 1994
Capital under management

Source: Created from data collected by the NVCA
Number of VC Funds

Source: Created from data collected by the NVCA
Number of companies being financed by venture capital

Source: Created from data collected by the NVCA
VC disbursements

Source: Created from data collected by the NVCA
VC funds are changing

- Average fund size no longer growing
- Size of investment rounds remaining stable
- Investments starting to move back to earlier stages?
- Corporate venture capital has pulled back to historical levels
Average fund size

Source: Created from data collected by the NVCA
Size of initial and follow on rounds

Average initial round of investment in millions of real dollars
Average follow on investment in millions of real dollars
5 per. Mov. Avg. (Average initial round of investment in millions of real dollars)
5 per. Mov. Avg. (Average follow on investment in millions of real dollars)

Source: Created from data collected by the NVCA
Movement back to seed and start-up stage deals?

Source: Created from data collected by the NVCA
Corporate Venture Capital Back to Historical Levels

Source: Created from data collected by the Pricewaterhouse Coopers MoneyTree Report and Thomson Reuters
The problem: No good substitute for venture capital

- Venture capital is important for building high growth companies
  - VC backed 150X more likely than average start-up to create jobs
  - VC-backed account for 10% of sales and private employment, but well less than 1 percent of companies
- No good substitute for venture capital
  - Not angel groups: In 2008, average VC investment was $7.4 million, but average angel group investment was only $275,000, and angel groups made only 1/4 the investments of VCs
  - Not individual angels: Average individual angel investment is only $77,000, half of individual angel capital is provided as debt, and more than 2/3 of individual angels are unaccredited
- Not debt providers: Providing appropriate rates of return using debt would violate usury laws.
And angel groups are getting pickier

Source: Created from data compiled by Angelsoft
What happens if VC market doesn’t come back?

• Fewer firms that need substantial equity investments to grow rapidly will get financing.
• That could mean fewer successful companies like Google and Genentech that provide innovative products that are valuable for all of us.
The $64,000 questions

• Are the trends in the venture capital industry a result of the financial crisis, structural changes, or just regression to the mean?

• What, if anything, can be done to get the industry back to its form in the golden years of the 1990s?