



State of the Markets

Outlook on the health and productivity
of the innovation economy

H2 2022



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Persevering Through a Downturn

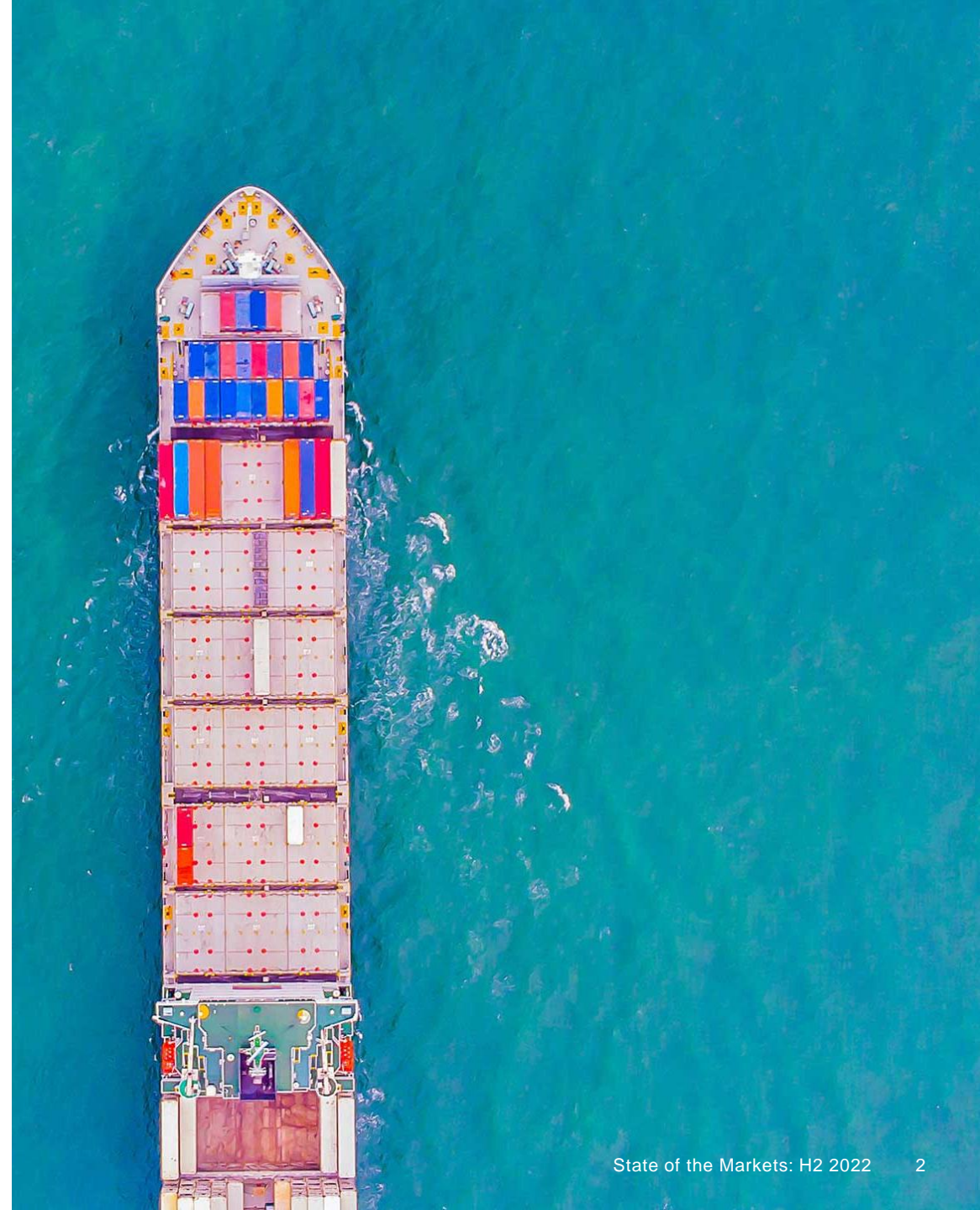
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Executive Summary

Persevering Through a Downturn

After two fantastic, record-breaking years for venture, the weight of macroeconomic conditions, geopolitical uncertainty and the lasting shadow of the COVID-19 pandemic have taken a toll. In the US, supply chain pressures drag on, inflation is just off a 41-year high, and interest rates are expected to continue rising. With these bearish indicators, public markets have reacted accordingly. Venture-backed tech companies that went public in 2021 have seen their revenue multiples decline 62% since the January 3rd market peak, and private valuations are beginning to follow suit.

With this backdrop, founders need to quickly adapt to the new normal by making quick decisions or risk missing milestones that could make future raises more difficult. Investors throughout Q2 have echoed the importance of reducing burn rates to extend runway and set a path to profitability. With revenue growth rates slowing, the profitability of private companies — not yet offset by lower cash burn — have deteriorated.

However, there are reasons to be optimistic. US venture capital (VC) fundraising is on track to have a record year and US VC investment its second-best year. Early-stage activity is robust, with 5,350 US VC deals in the first half alone — in line with 2021's record year. In some ways, the COVID-19 pandemic prepared companies for this downturn. They hold more cash, and many have been through the cost-cutting drill once before. Ultimately, less competition for talent, increased potential of consolidation, and an anticipated prolonged period of growth following an economic slowdown may present opportunities for many VC-backed companies. Many notable companies have been founded during a downturn, as we saw in 2008, and many established companies will continue to grow and come out stronger on the other side.

It is with this in mind that while we are cautious in the short term, we are optimistic in the long term.

Mike Descheneaux
President

Sunita Patel
Chief Business Development Officer





Macro:

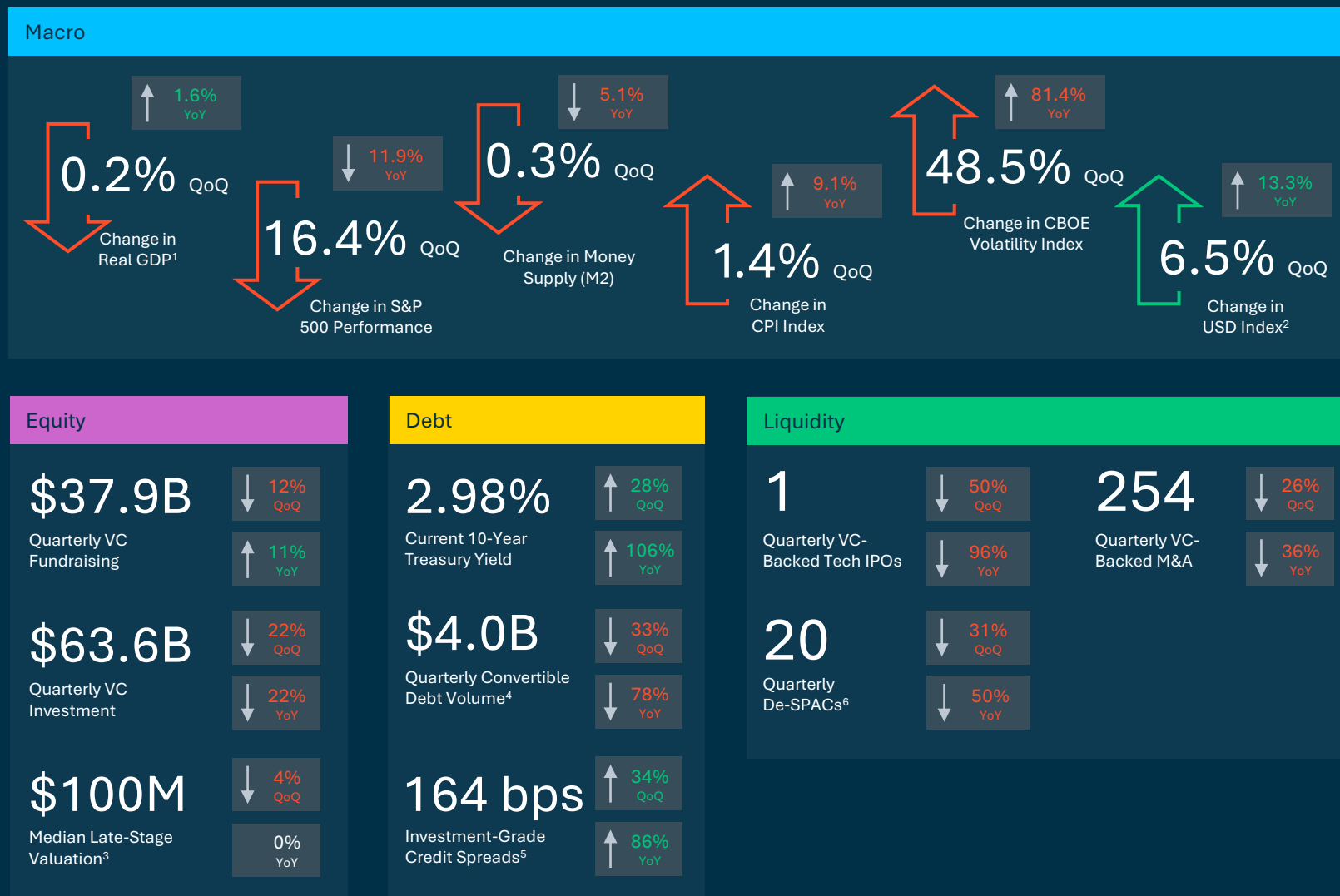
Persevering Through a Downturn



US Innovation Economy Indicator Dashboard: Q2 2022

While GDP had its second successive quarter of decline in Q2, it is important to note that GDP is still up year-over-year (YoY). The S&P 500 is down 12% YoY (from a record-setting 2021) as inflation continues to be elevated. The VIX, a measure for market volatility, is elevated. As such, the IPO market is effectively shut until there is more price stability. However, when things do settle down, a large pipeline of VC-backed companies will likely be ready to exit.

As prices across the board rebase, acquirers are biding their time, as evidenced by the slowdown in M&A deals following a record 2021. VC fundraising and investment fell QoQ, but are both on track for above-average years. Perhaps most importantly for a positive long-term outlook, the innovation economy is on pace for its second-best year, with strong activity at the early-stage as the next cycle of startup formation begins.

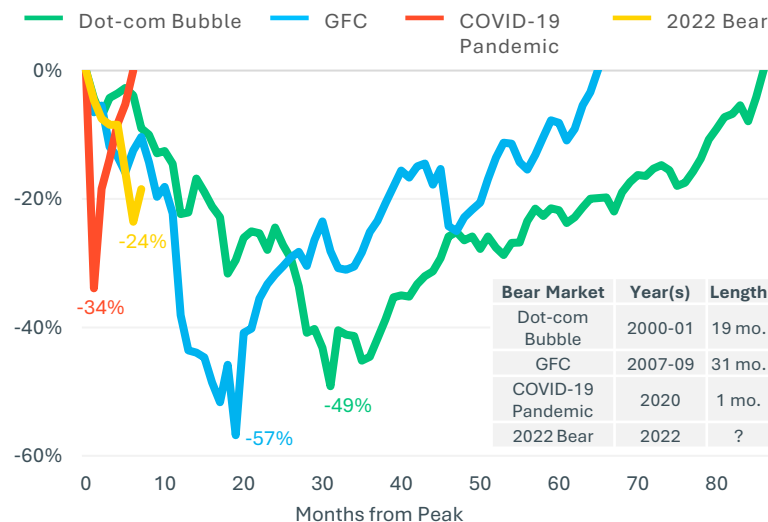


Grin and Bear It

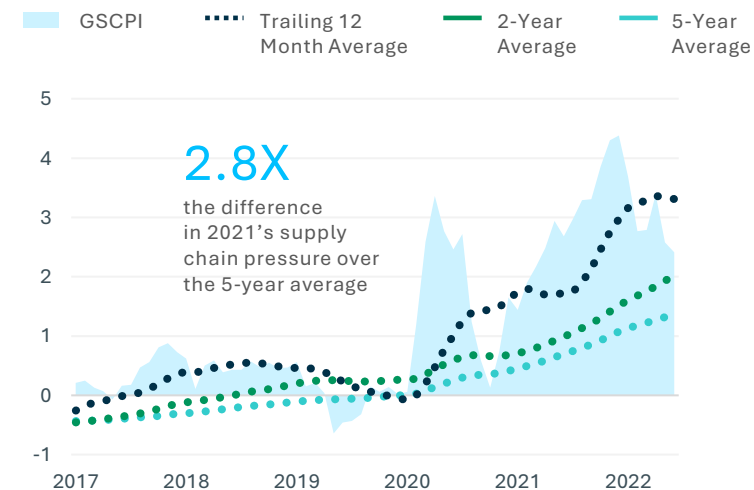
Following two years of stimulus-fueled growth, the US is heading into an economic correction. The S&P 500 — which hit 70 all-time highs in 2021 — was down 21%, as of June 30, from its peak on January 3. Supply chains — strained by inflated consumer demand, worker shortages and pandemic-related shutdowns — are still gridlocked and continue to hamper global trade. The Fed has been actively raising interest rates, with the Fed funds rate rising from 0.08% in February to 2.33% as of August 1st. Inflation reached a 41-year high of 9.06% in June, before declining to 8.50% in July.

Looking at the trajectory of the 2022 downturn and considering the yet-to-be-resolved drivers such as supply chain delays, the war in Ukraine and the COVID-19 pandemic, it's feasible that a recovery could take longer than a year. The Global Financial Crisis (GFC: 2007-2009) lasted 19 months followed by a 46-month recovery. However, companies are better positioned today for a prolonged downturn than they were entering the GFC. Corporate balance sheets are generally in good shape after years of low interest rates and rising asset prices.

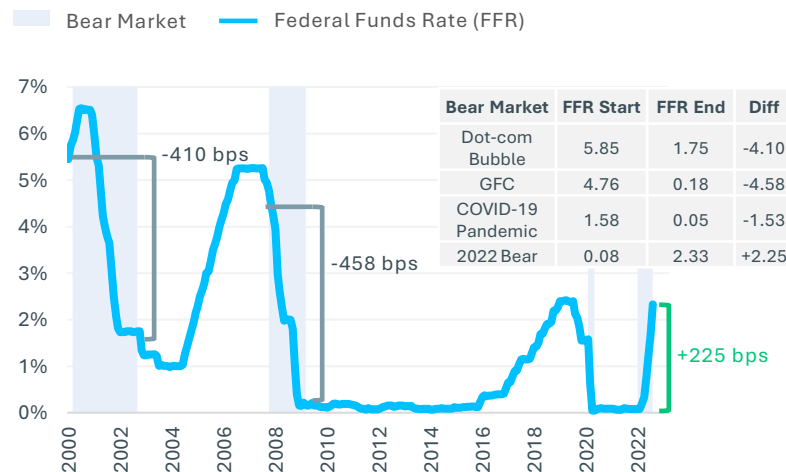
S&P 500 Returns Through Bear Markets¹



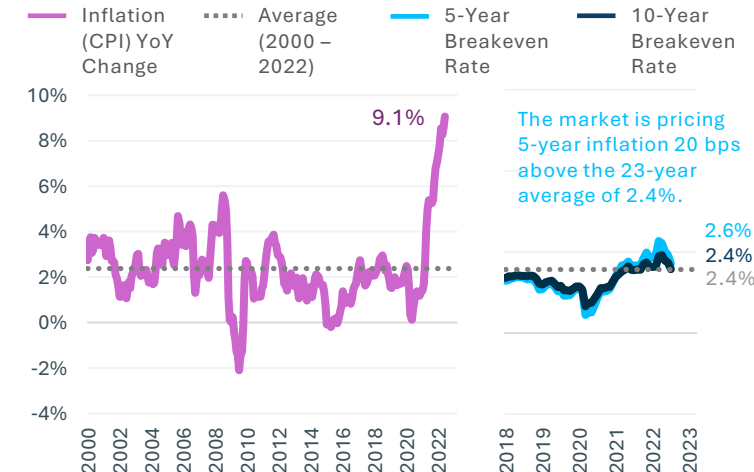
Global Supply Chain Pressure Index (GSCPI)²



US Federal Funds Rate Through Bear Markets³



Inflation: Actual and Breakeven Rate⁴



Notes: 1) As of 8/1/2022. S&P 500 values indexed to the peak daily settlement price before the downturn. Values are aggregated to a monthly average, except for the peaks and troughs, which are the actual daily settlement values. 2) An index from the New York Fed that incorporates several indicators of supply chain disruption. 3) One basis point (bps) is equivalent to 0.01%. 4) CPI values are seasonally adjusted. Projections are a measure of expected inflation derived from the spread between Treasury bonds and inflation-protected bonds of the same maturity.

Source: S&P Capital IQ, St. Louis Fed, New York Fed and SVB analysis.

A Step Back, but Many Steps Ahead

At the onset of the GFC, Sequoia Capital saw what was to come and created the now oft-quoted “RIP Good Times” presentation for its portfolio companies. The advice given to founders was to adapt quickly, bolster their balance sheets and “spend every dollar as if it were your last.” VCs are echoing a similar sentiment today, urging founders to cut costs and preserve capital to maximize runway.

The pace of venture investment in 2022 has slowed, and late-stage tech valuations have dropped. To understand potential paths forward, we analyzed both measures through prior bear markets: the dot-com bubble and the GFC, beginning in 2000 and 2008, respectively.

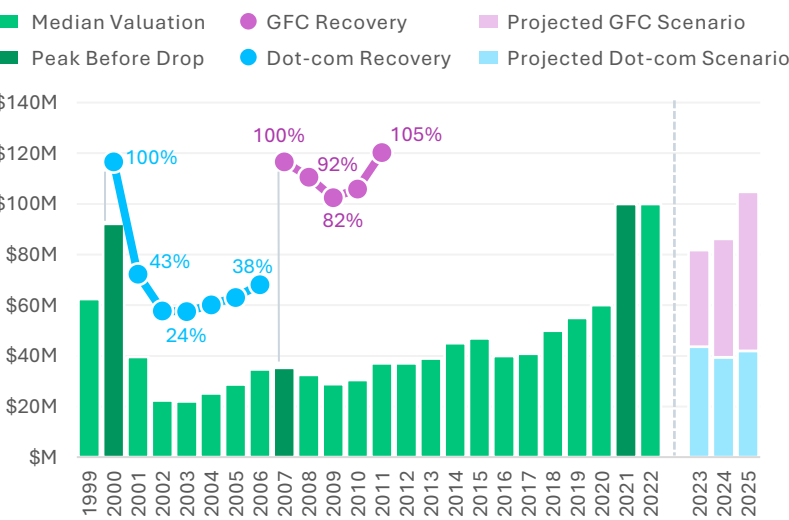
The innovation economy today is better equipped to weather the impact of an economic downturn. Unlike in 2000, technology is highly adopted and is inherent in nearly everything we do. Tech companies have solid fundamentals, new markets and industries have emerged, and VC is becoming steadily institutionalized. This is evidenced by the asset class becoming increasingly correlated (nearly 1:1) with the S&P 500 Index, which also recognizes the size and number of tech companies represented in the index. Even factoring in a dot-com or GFC correction scenario, the level of VC investment will be at least in line with recent years (excluding 2021).



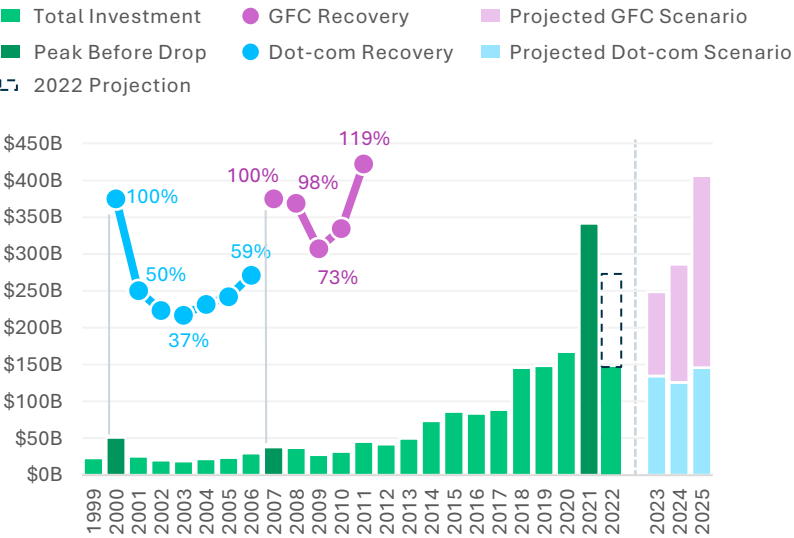
Notable VC Guidance to Founders¹

VC Firm	Prioritize Growth or Runway?	Runway Target	Key Insight
SEQUOIA	Runway	24+ months	“You’ll need a lot more runway than you think.”
Y Combinator	Runway	24+ months	“Pick up market share by staying alive.”
CRAFT	Runway	30+ months	“Extending runway trumps growth rate right now.”
Lightspeed	Runway	24+ months	“Cut non-essential activities.... Focus on good unit economics.”

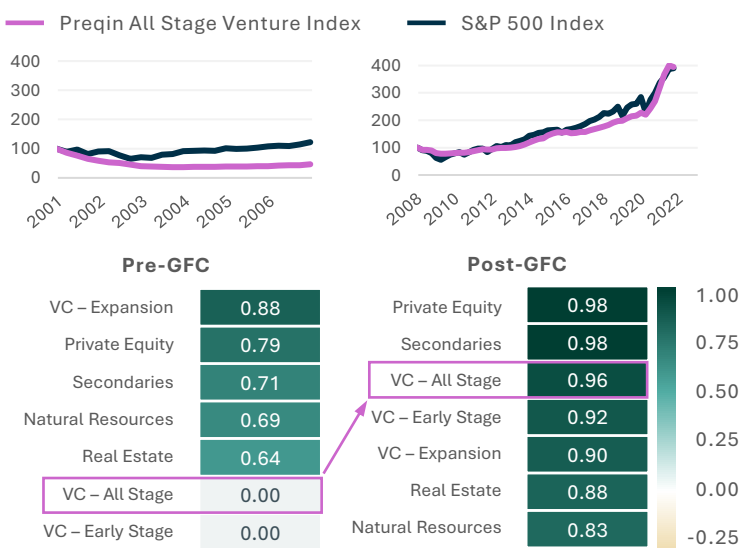
Median Late-Stage Valuations: Actual and Projected³



US VC Investment: Actual and Projected²



S&P 500 Index Correlations by Asset Class⁴



Notes: 1) Guidance pulled from presentations and press releases published by selected firms in May 2022. 2) As of 7/7/2022. Extrapolated value based on an exponential smoothing forecast of monthly data. 3) Pre-Money Valuations as of 7/7/2022. 4) Correlations provided as R-squared values. An R-squared of 1 indicates movements in the S&P 500 explain 100% of the variance in a correlated asset. Private equity (PE) excludes VC funds. Source: PitchBook, Prequin, press releases and SVB analysis.



Capital:

The Next Wave of Venture Is Born



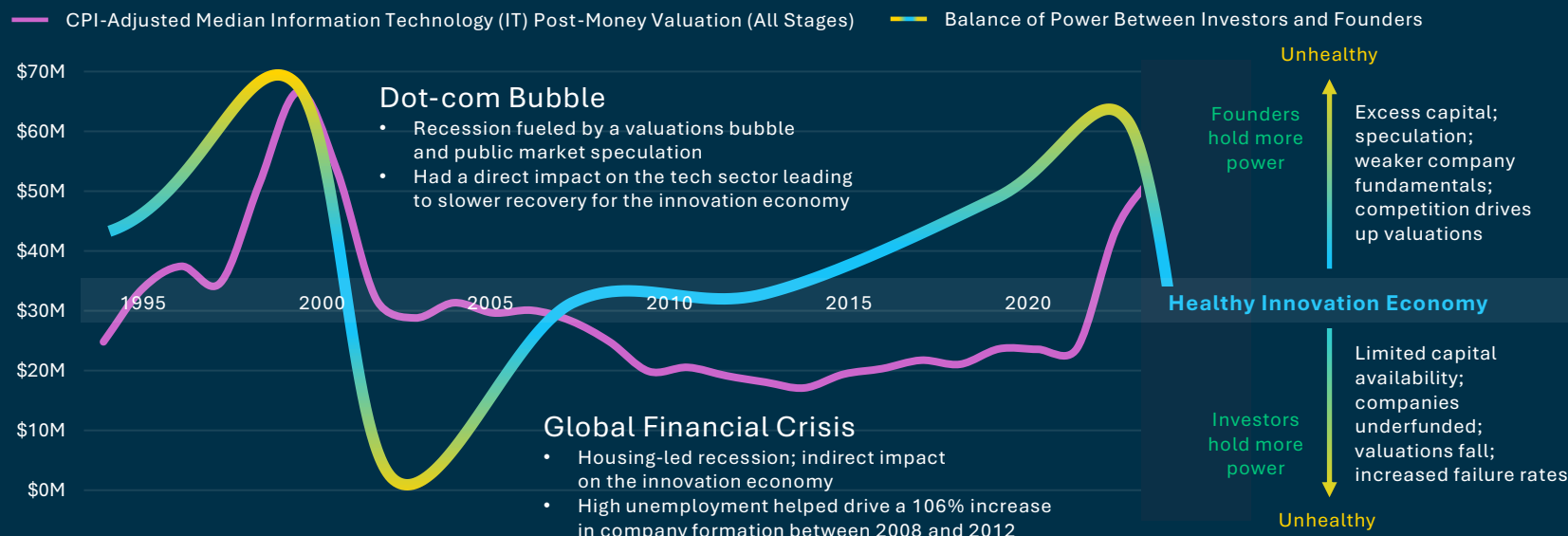
Returning to a Healthy State

In the frenzied environment of 2021, VC activity surged, and the competition to get in on the best deals put many founders squarely in the driver's seat to command outsized valuations. Check sizes rapidly increased as well as the speed of decision-making and due diligence. Heightened competition pushed up the median late-stage pre-money valuation by 67% YoY to \$100M in 2021, a level (when adjusted for inflation) we haven't seen since the dot-com bubble. Public markets started to cool at the turn of the year.

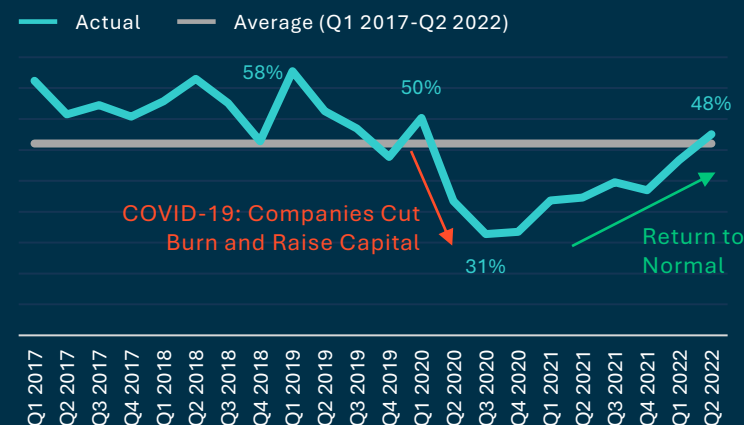
The S&P 500 and Nasdaq-100 tech indices are down 21% and 35%, respectively, from their all-time peaks in 2021. Private markets began to adjust, and in turn VC investment slowed down from the dramatic pace of 2021.

In this new normal environment, founders should look to balance the need to raise capital against increased dilution. The prospect of raising money at a lower valuation (a down round) can trigger anti-dilution terms that typically take value away from early investors and employees. However, raising a down round isn't as bad as many assume. Rebasings a company's valuation can relieve the burden placed on a founder to grow rapidly by spending on headcount, sales and marketing all in the hope of taking substantial market share. With less excess capital available, a more considerate and planned approach to growth can be taken, reducing inefficiencies that can creep into a fast-growing business.

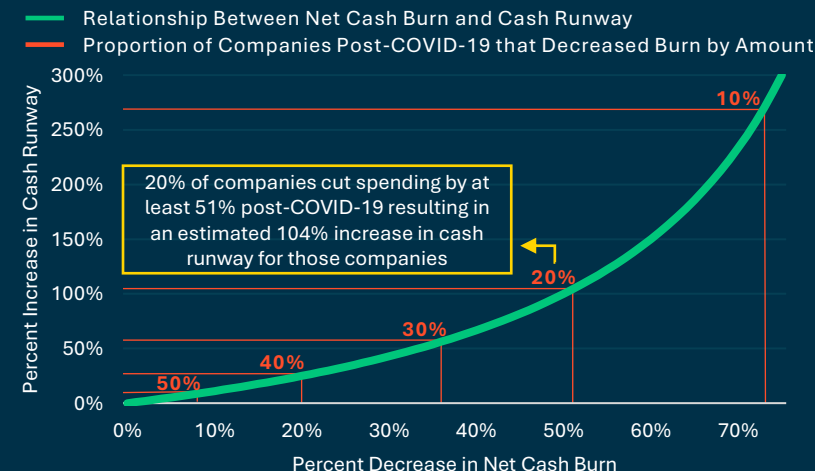
Venture Fundraising Balance of Power: Correlation to Private Information Technology Valuations



Proportion of US VC-Backed Tech Companies with Less than 12 Months of Runway¹



Change in Net Cash Burn and Expected Impact on Cash Runway²



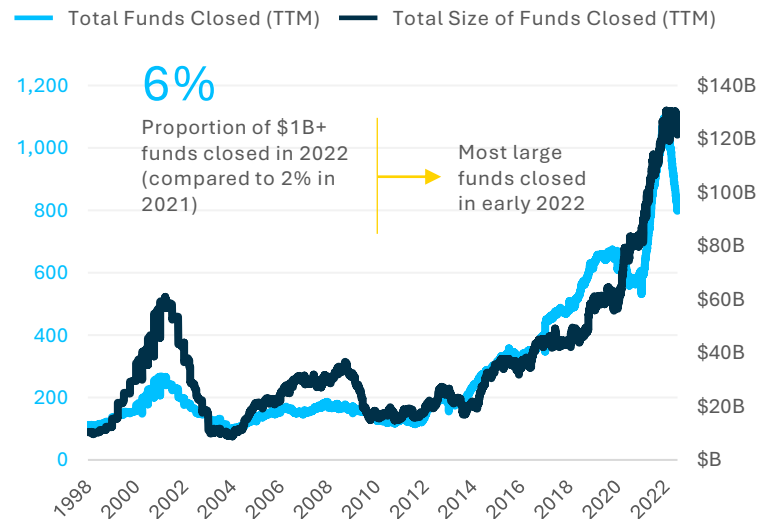
Dry Powder Ready and Waiting

By H1 2022, nearly \$82B in US VC funds had been raised — the highest amount over a six-month period. Following the record breaking year that was 2021, it signals that both limited partners (LPs) and VCs see continued opportunities across the innovation economy. As early as 2019, the amount of capital raised by VCs had surpassed the dot-com bubble, before skyrocketing at the onset of the COVID-19 pandemic. Low interest rates drove investors away from traditional assets such as bonds, and towards the high-risk/high-return world of venture. This included the rise of the “hybrid” investor. VCs were investing at a rapid pace and at sky-high valuations, which meant they had to raise larger funds at a quicker pace (many within 12-15 months). Between 2019 and 2021, the median time between funds decreased by five months to 30 months for funds over \$100M. In turn, LPs — buoyed by strong returns and the intense hype around tech — upped their allocations. For example in 2021, the CalPERS board moved to increase its allocation to venture from 8% to 13%, starting July 1, 2022. As a result of these dynamics, VC funds have nearly \$269B in dry powder to deploy.

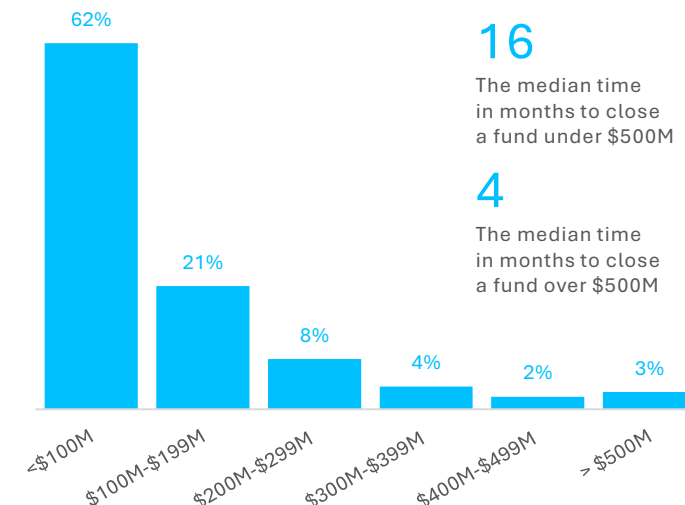
Many VCs are cognizant of the pressure LPs are facing with regards to the market downturn, choosing to preserve their relationships by avoiding calling capital prematurely, especially when they are unsure if valuations will continue to rebase. While the innovation economy sits on record dry powder, the rate of deployment may slow. Consider \$1B+ funds — accounting for 40% of dry powder — which have cut investment by 88% between June 2021 and June 2022. These funds are overwhelmingly investing in late-stage companies. Yet not all VCs are reacting as quickly, with some investors recognizing that early-stage companies are more sheltered from market pullbacks and so have not seen the significant drop the \$1B+ funds witnessed.



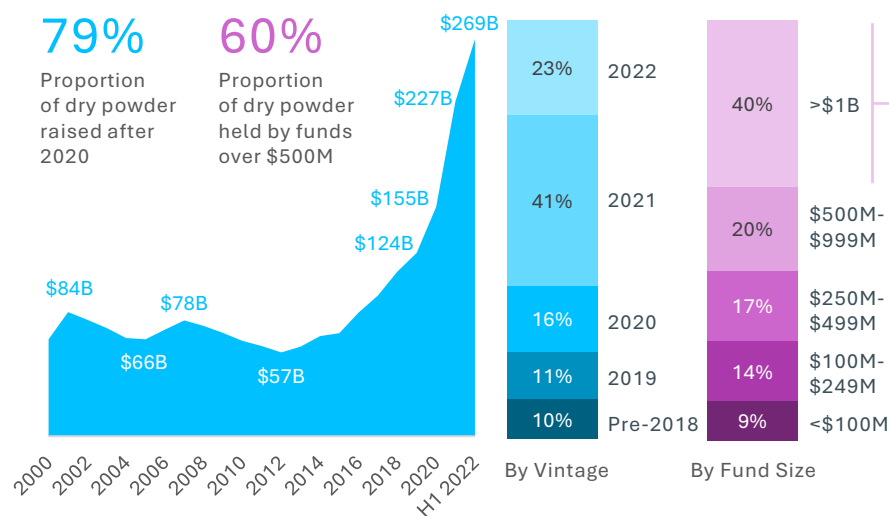
US VC Fundraising



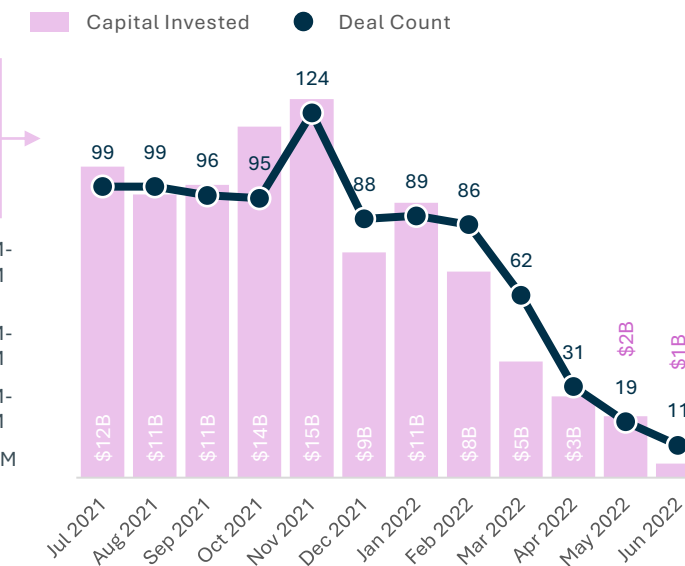
Distribution of US VC Funds Raising Capital by Fund Size¹



US VC Dry Powder by Vintage and Fund Size²



US VC Investment by \$1B+ Funds



Notes: 1) Funds that are actively raising and have not reported a final close.
2) Data is reported as a point in time: H1 2022 as of 6/30/2022; all other as of year end.
Source: Preqin, PitchBook and SVB analysis.

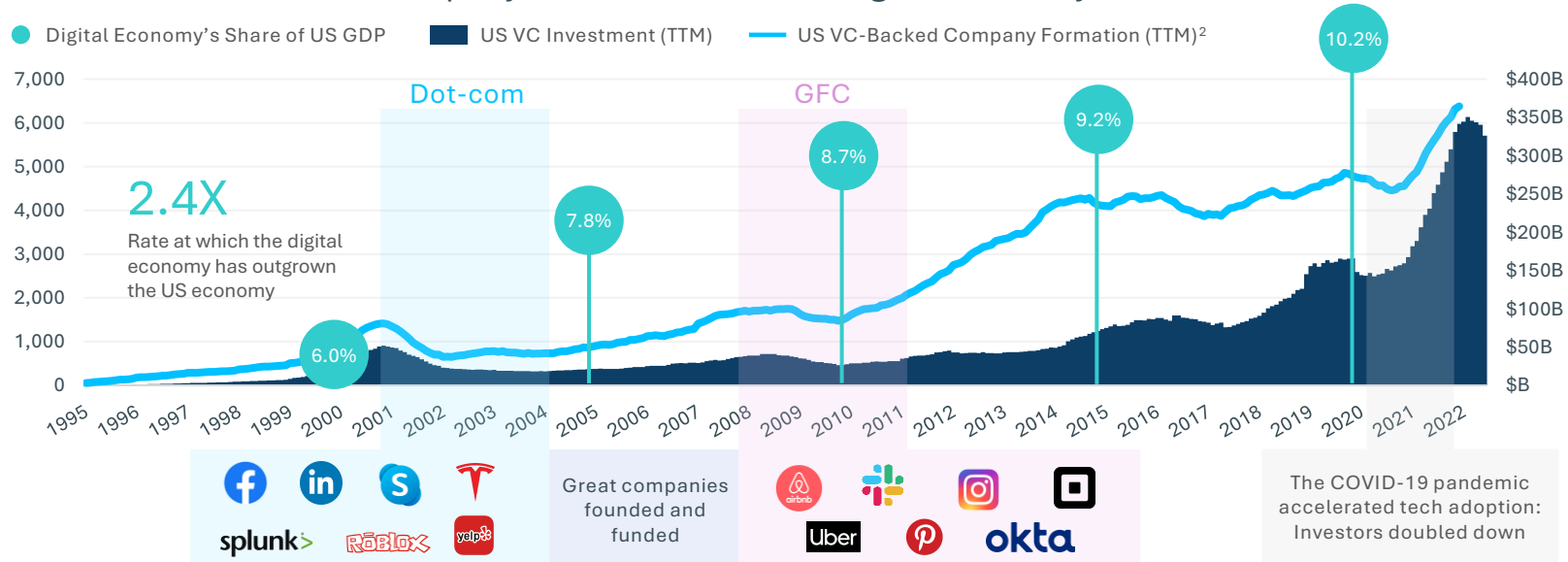
Innovation Thrives Amid Adversity

The US innovation economy has grown at twice the rate of the global economy since the mid-1990s. Tech is no longer a vertical, but a horizontal used across every aspect of the economy. As a result, technology may be less impacted than in past cycles. The year after the dot-com bubble burst, US VC investment dropped 50%. If a similar drop were to happen this time around, US VC tech investment would only reset to 2020 levels, the second-highest year for venture investment. While investment may take time to return to its previous peak (it took 13 years after the dot-com bubble), we expect company formation to remain resilient. The COVID-19 pandemic accelerated digital adoption to an unprecedented degree, which proliferated the number of opportunities available for entrepreneurs. US-based founders started 6,400 companies in 2021, a record for any 12-month period and more than double the amount started in 2019.

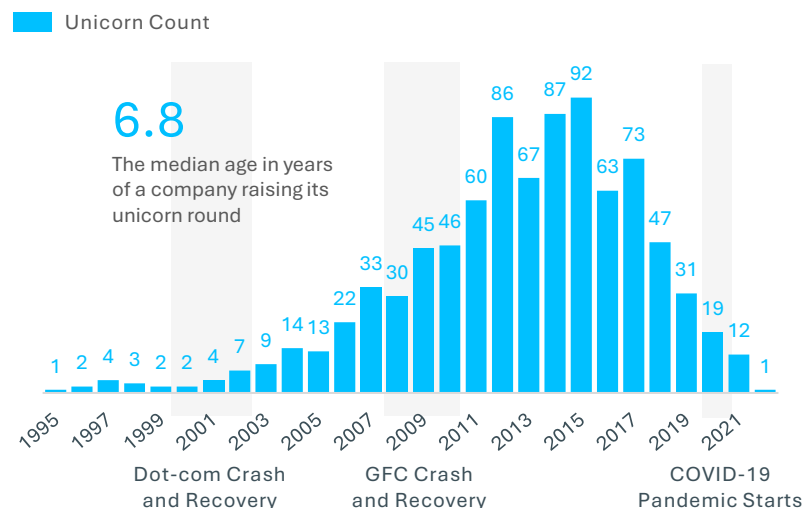
Downturns are generally favorable times for founders to start businesses. As startups cut costs, hiring falls and layoffs rise, leading to a lower opportunity cost to start a business. Top tech talent, who benefitted from a record exit environment in 2021, have substantial capital available. This has manifested in starting businesses, angel investing or both. Either way, capital is being returned to the ecosystem, spurring the next wave of innovation. This trend is similar to the dot-com and GFC periods when many notable companies were founded. We are witnessing a slowdown in VC activity. This has resulted in a lower supply of capital for companies looking to bolster their balance sheets before a downturn. An artifact of this slowdown has been a slight drop in the number of unicorns christened: 141 in H1 2022 compared to 188 in the back half of 2021.



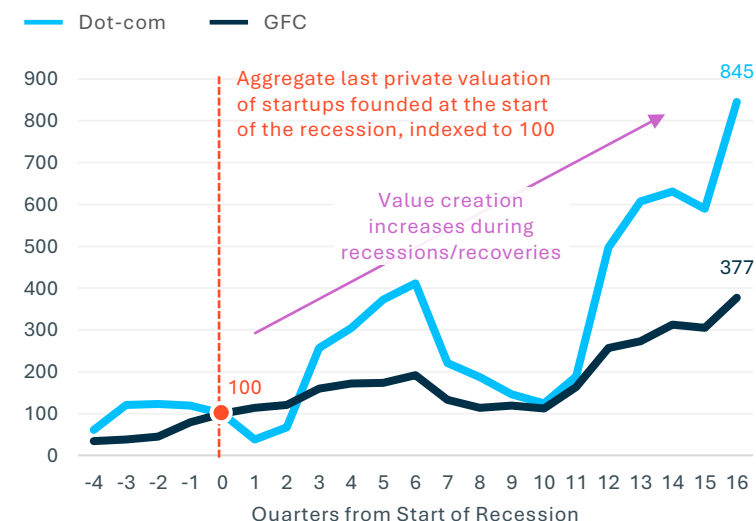
US VC Investment and Company Formation, and the Digital Economy's¹ Share of US GDP



US Unicorns by Year Founded³



Value Creation Index by Recession⁴



Notes: 1) Digital economy defined by the US Bureau of Economic Analysis (BEA) and used as a proxy for the value added to GDP by that sector. 2) First VC round raised used as a proxy for company formation. 3) Unicorn data provided by PitchBook; includes US VC-backed companies that have reached and maintained at least a \$1B post-money valuation. 4) The sum of the aggregate LPV for the trailing 365 days, smoothed using a 3-month moving average and indexed to 100 at the start of the recession, as defined by the National Bureau of Economic Research (NBER). Source: PitchBook, US BEA and SVB analysis.



Investment: Deal Dynamics Shift

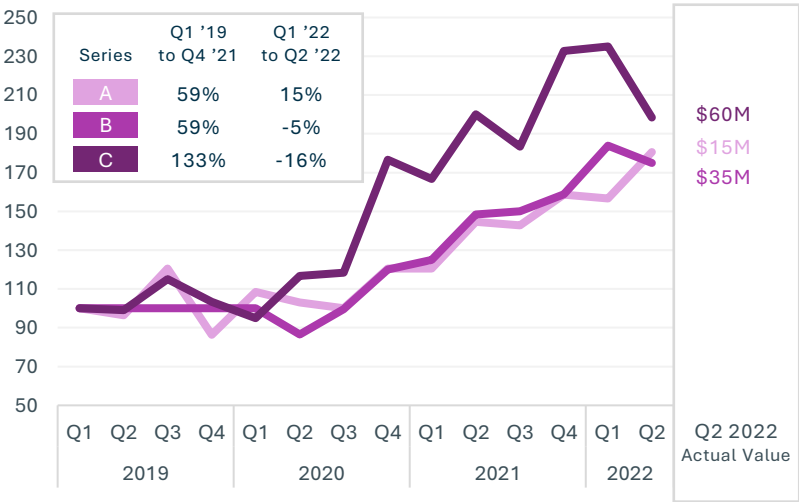


Valuations at an Inflection Point

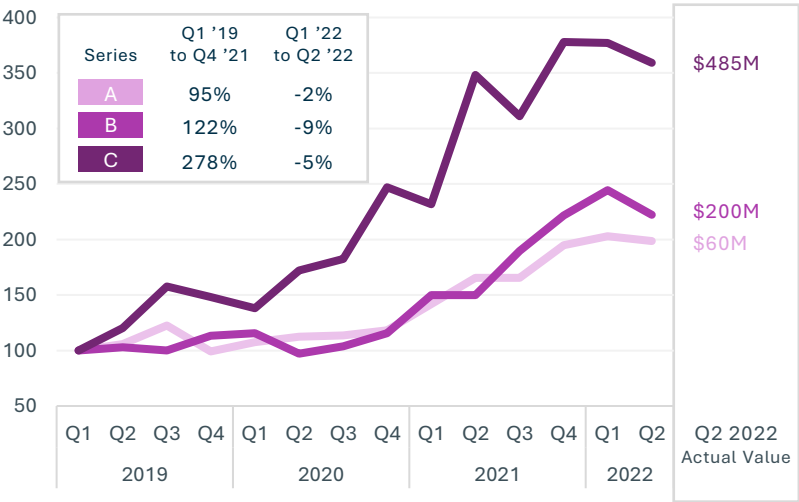
In Q2 2022, deal sizes and valuations showed signs of moderating, but are still pacing well above pre-pandemic levels. Given the position of strength from which the innovation economy is starting, a precipitous drop is unlikely. For valuations to return to 2019 levels, Series A valuations would need to fall 49%, Series B by 55% and Series C by 72%, which are drastic declines. Early-stage valuations should remain resilient, especially compared to late-stage valuations, as they are not compared to public company fundamentals.

The extent and rate of changes in deal pricing are unclear, so it is key that founders heed the advice of their investors and preserve their balance sheets at all costs. As previously noted, post-GFC the correlation between public markets and Preqin's Venture Index (the primary component of which is fund-level net asset value [NAV]) has been high ($R^2=0.96$). While lagging, it is important for private companies (especially at the late-stage), to keep a pulse on price movement of comparable public companies.

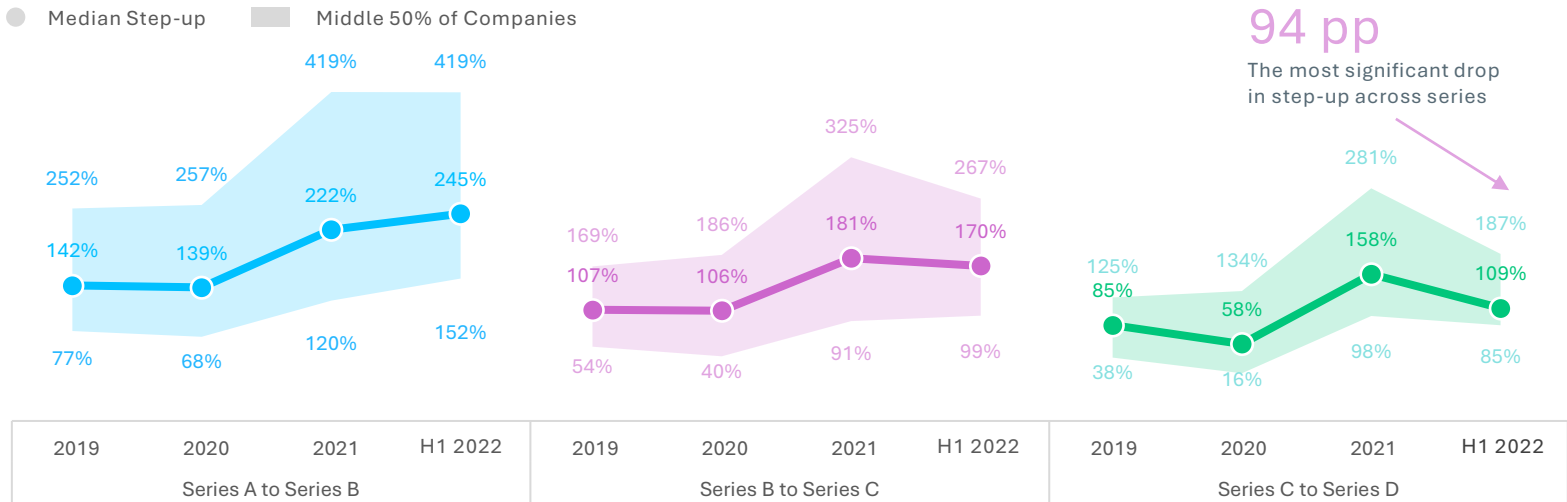
US VC-Backed Tech: Median Deal Size Indexed to 100^{1, 2}



US VC-Backed Tech: Median Post-Money Valuation Indexed to 100^{1, 2}



US VC-Backed Tech: Valuation Step-up by Series^{1, 3}



Notes: 1) Tech defined using SVB's proprietary taxonomy. 2) Indexed to 100 in Q1 2019. 3) The median percentage increase from the post-money valuation of the prior round to the pre-money valuation of the next round.
Source: PitchBook and SVB analysis.

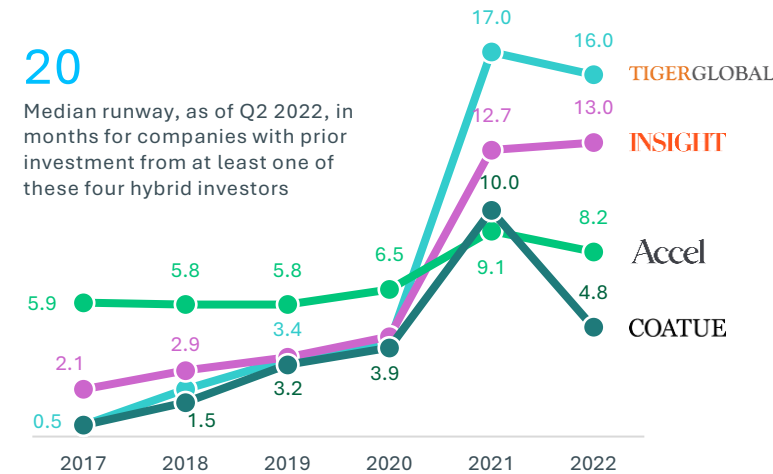


Hybrids Refocus on the Early-Stage

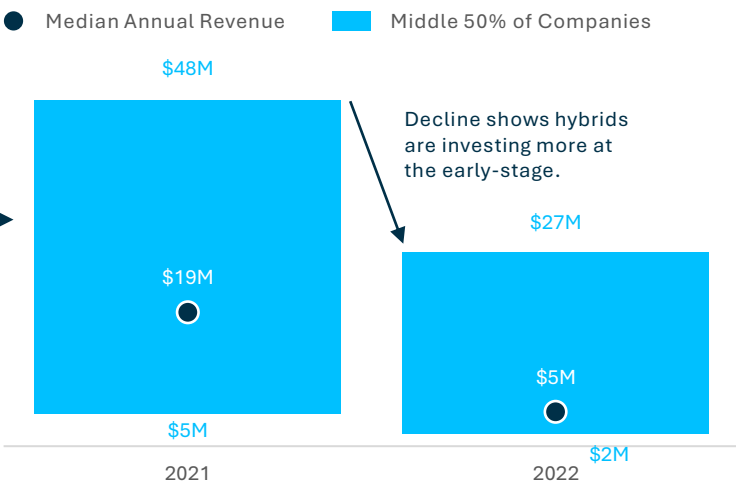
The entrance of “hybrid” investors fundamentally changed the venture landscape, pushing the pace and size of venture investments. This resulted in multiple epochs for venture, starting in 2014 when investment jumped from \$49B to \$75B, stepping up to \$145B in 2018 and finally culminating with \$341B in capital deployed in 2021. With massive capital pools behind them, hybrids deployed larger check sizes pushing up valuations. The downturn in public markets led to price drops in hybrids’ portfolios — both public and private. As such, hybrids have slowed their late-stage investing and are increasingly active at the early-stage, which has historically been more insulated from public market tumult.

As capital allocators hit pause and valuations rebase, companies risk running out of runway. A valuation overhang creates a decision for founders, who could either raise a flat round or down round, cut expenses to reach break-even or extend the company’s runway by using non-equity financing. The impacts in each scenario need to be comprehensively understood. This might be one reason why interest in debt financing has steadily increased: Debt can be utilized by a company to provide the additional time needed to grow into its last private valuation.

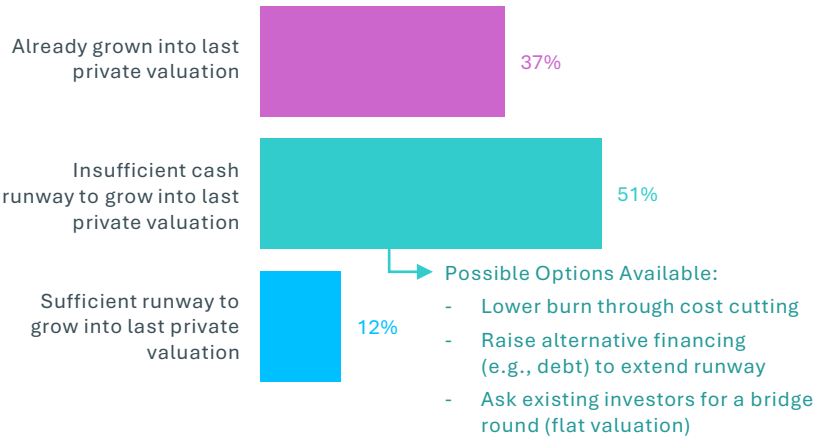
Average Number of Closed Deals per Month by Select Hybrids¹



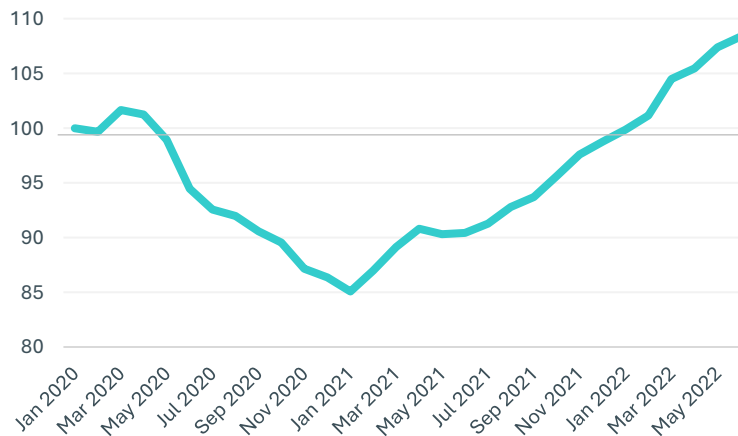
Hybrid Investments: Annual Company Revenue²



Analysis: Distribution of Outcomes if Revenue Multiples Decline to 2019 Levels³



Growth-Stage Tech Company Interest in Debt (Indexed to 100 on 1/1/20)⁴



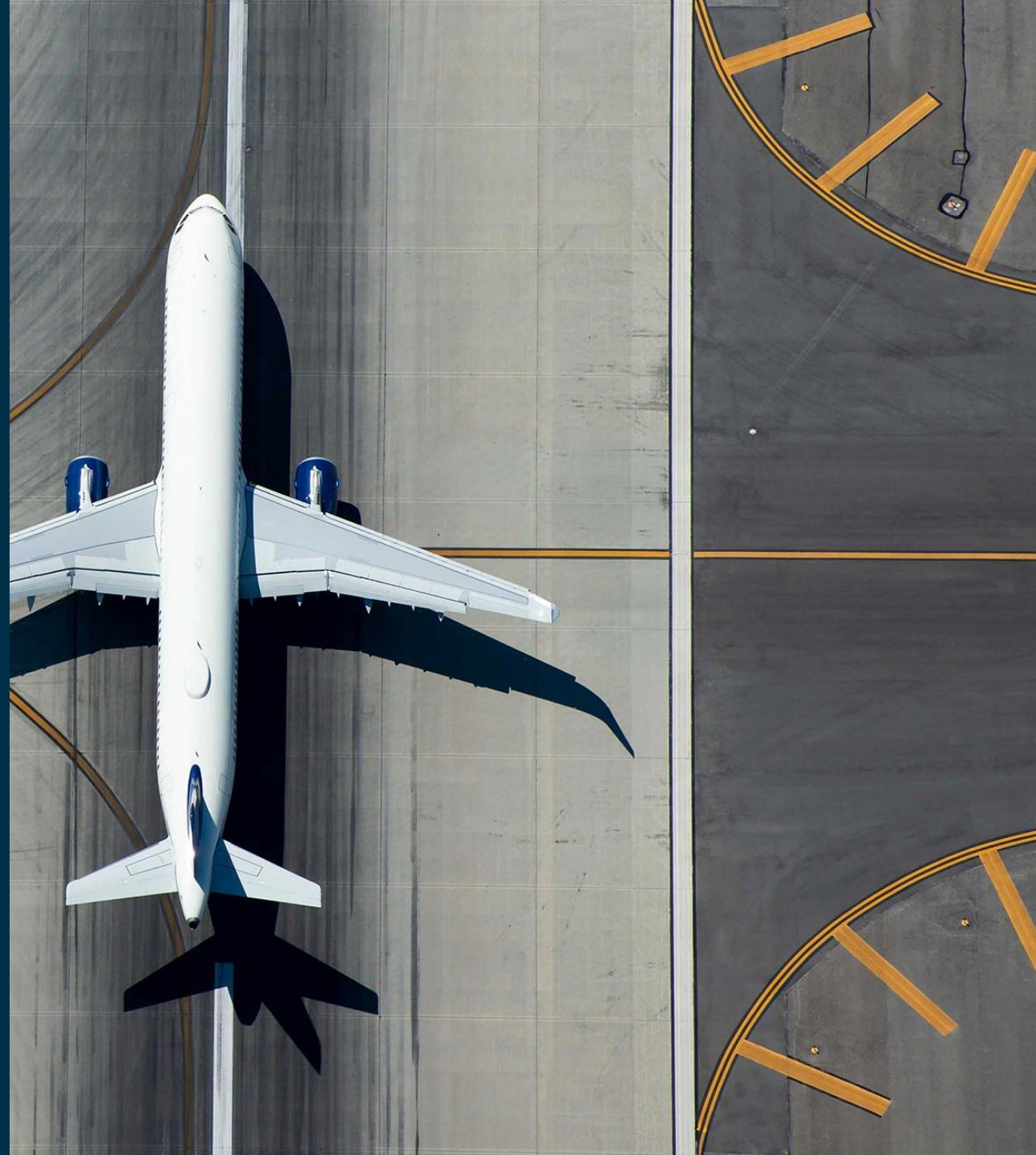
Notes: 1) A fund that has characteristics of a PE and VC fund. 2) Based on investments by Tiger Global, Insight Partners, Accel and Coatue; annual revenue calculated using the run rate of revenue for the year of the deal; 2022 using H1 data. 3) Created an implied revenue multiple for each company based on revenue, sector and growth rate compared to 2019 multiples for similar companies; compared this multiple to the multiple they received in their last round and assumed current revenue growth rates to calculate the time required to grow into the implied multiple. Compared this time to company runway. 4) Based on number of debt inquiries by US tech companies.

Source: PitchBook, SVB proprietary data and SVB analysis.



Benchmarking:

Model Companies Work on Runway



Top Line, Meet Bottom Line

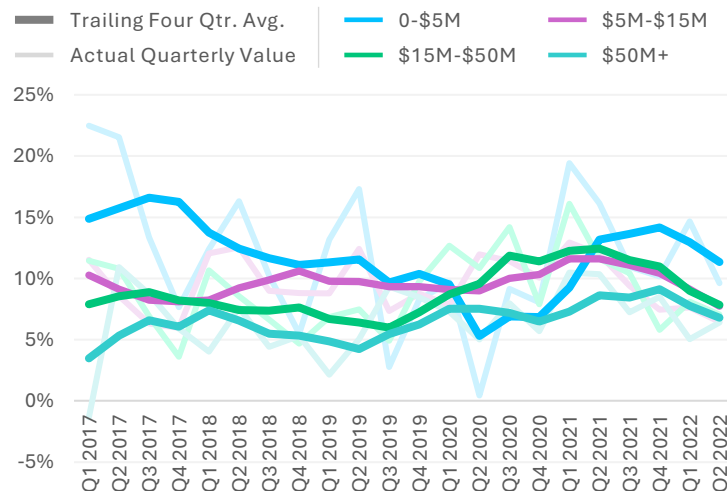
Early in 2020 when COVID-19 lockdowns started, Sequoia Capital, one of the most prominent VC firms, published its “Black Swan” letter urging founders to act fast to preserve cash. Layoffs spiked, with companies reacting quickly to cut their largest expenses. Founders had good reason to worry. Consumer spending, historically an up-and-to-the-right metric, plunged an unprecedented 18% between February and April 2020. The S&P 500 dropped 34% from its peak, and the general sentiment was one of uncertainty. As a result, median revenue growth rates dropped across tech. However, the decline didn’t last long. Government stimulus fired the economy back up, as businesses quickly adapted to the new normal. Growth rates for most tech companies — apart from those directly impacted by shutdowns — rebounded and for some accelerated.

Enter 2022: Public markets fell, GDP in Q1 and Q2 2022 declined, and inflation continued to rise, seemingly immune to Fed interest rate hikes. Unsurprisingly, revenue growth rates are beginning to drop again. Prominent VCs are repeating their warnings for companies to extend runway and cut burn. The signs of a slowdown are already apparent with a greater proportion of companies seeing revenues fall. Some sectors are more impacted than others. Consumer internet for example, has been hit hardest amid declining consumer confidence and slowing demand.

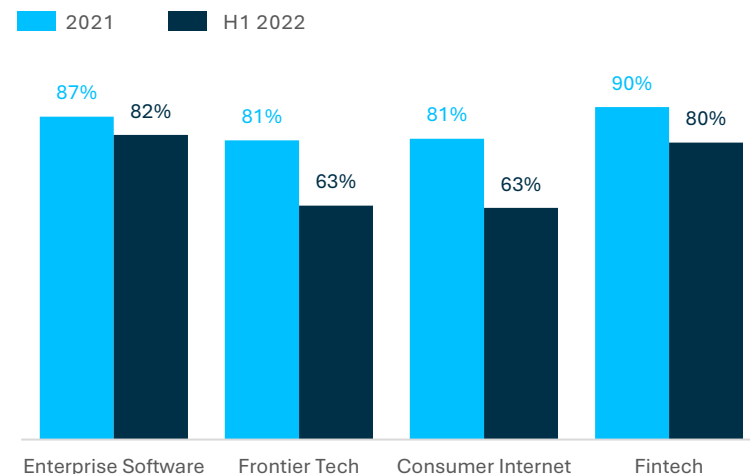
The efficiency gains that companies made at the start of the pandemic were cast aside as new and unexpected growth opportunities emerged. Now, companies are actively pursuing those efficiencies again, but due to the fixed nature of certain costs, such as payroll and office space, the resulting savings lag behind revenue changes. Based on trends in certain expense categories, we expect to see improvements in EBITDA margins in the coming quarters.



Median QoQ Revenue Growth Rate by Annual Revenue Band^{1, 2, 3}



Proportion of US VC-Backed Tech Companies with YoY Increasing Revenue^{2, 4}

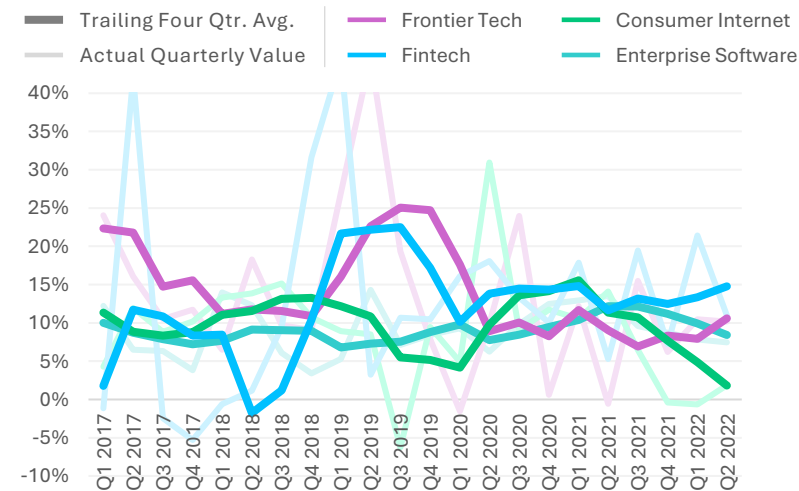


Notes: 1) Cohort is US VC-backed tech companies. 2) Tech companies as defined by SVB’s proprietary taxonomy. 3) Annual revenue calculated by multiplying quarterly run rate by four. 4) 2022 calculated using H1 2022 financial statements and projecting through end of year based on current run rate.

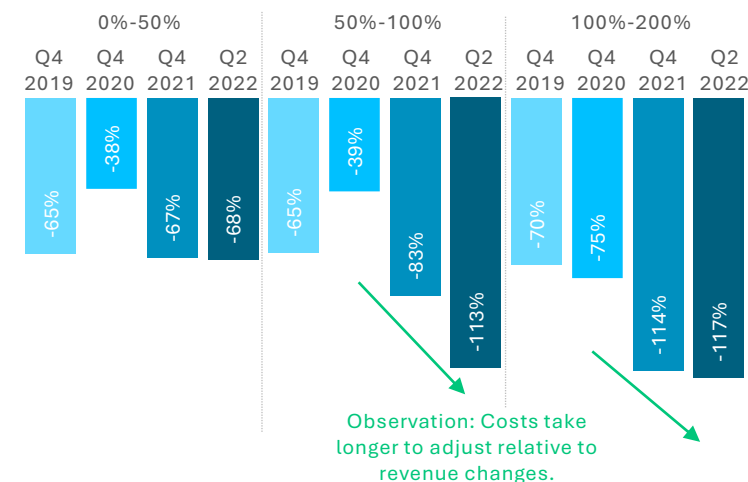
Source: SVB proprietary data and SVB analysis.

Median QoQ Revenue Growth Rate by Sector^{1, 2, 3}

Cohort: US VC-Backed Tech Startups with \$15-\$50M in Annual Revenue



Median EBITDA Margin by Revenue Growth Rate Band^{1, 2}

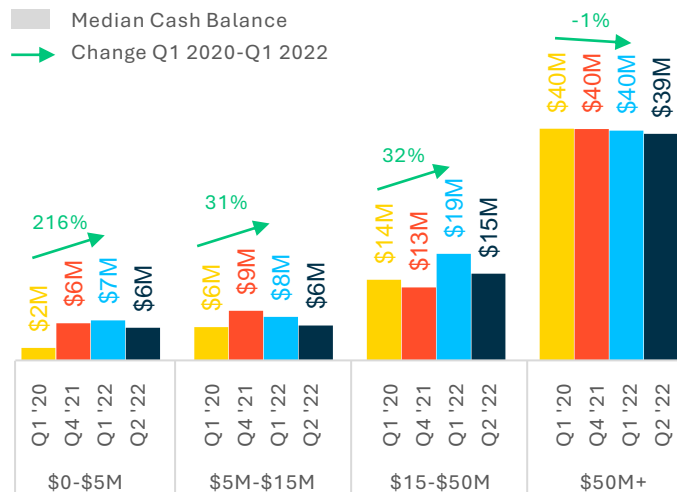


Slow Burn to Preserve Near-Record Cash

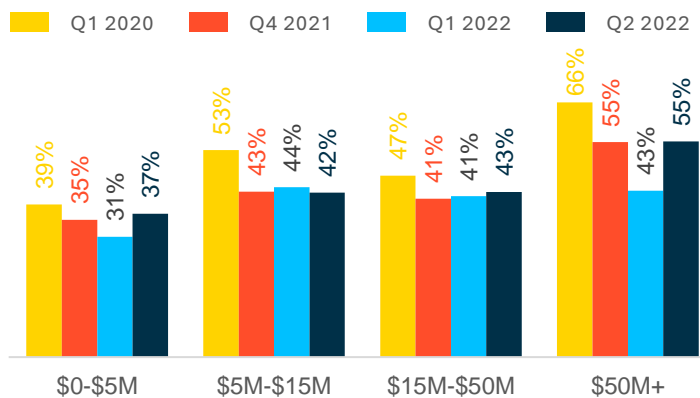
After the dust settled from the initial phase of the COVID-19 pandemic, the sentiment was: “We are going to be OK.” Many tech companies experienced a boost from the shift to remote work and record stimulus payments from the federal government. In 2021, the intense competitiveness of the venture market had investors preempting rounds, making concessions on terms and offering larger check sizes with expedited due diligence. Capital abundance encouraged companies to raise more capital and, in turn, hold more cash. At the start of 2022, US VC-backed tech companies held more cash than they had at the start of the COVID-19 pandemic; companies with \$15M – \$50M in annual revenue held 32% more cash. This is fortunate as we enter a downturn.

Based on the burn multiple analysis, companies are burning more cash per dollar of net new revenue than they have over the last five years. This results from two factors. First, companies were expected to put capital to work to grow. Second, revenue growth in 2022 slowed. This has created a timing imbalance between cost cutting and slowing revenue growth, presenting poorer fundamentals in the near term. To reduce dependence on uncertain equity markets, plotting a path to profitability is vital.

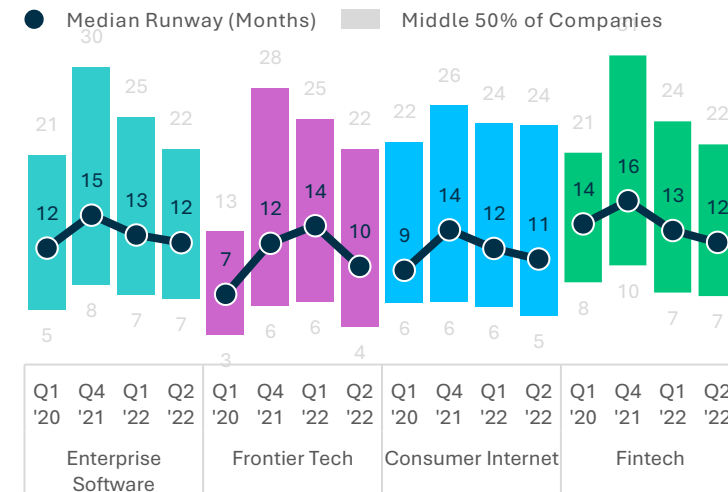
US VC-Backed Tech Companies Cash Balances by Annual Revenue Band^{1, 2}



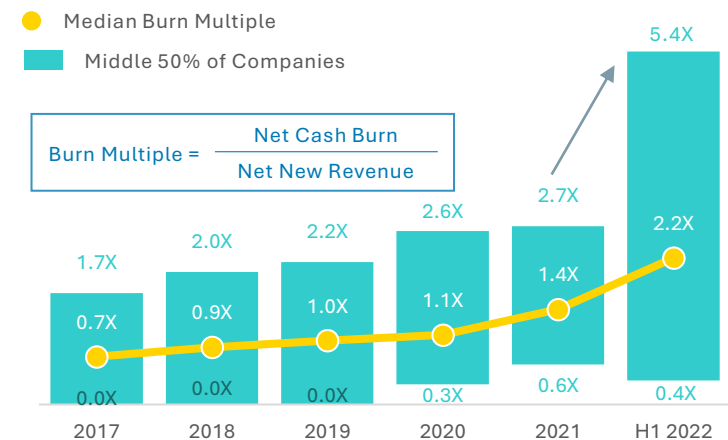
Proportion of US VC-Backed Tech Companies with Improving EBITDA Margins QoQ by Annual Revenue Band¹



US VC-Backed Tech Companies Cash Runway by Sector^{1, 3}



US VC-Backed Tech Companies Net Cash Burn Multiple^{1, 3}



Notes: 1) Tech companies as defined by SVB's proprietary taxonomy. 2) Annual revenue calculated by multiplying quarterly run rate by four. 3) Cashflow negative companies. Source: SVB proprietary data and SVB analysis.

Cutting a Path to Profitability

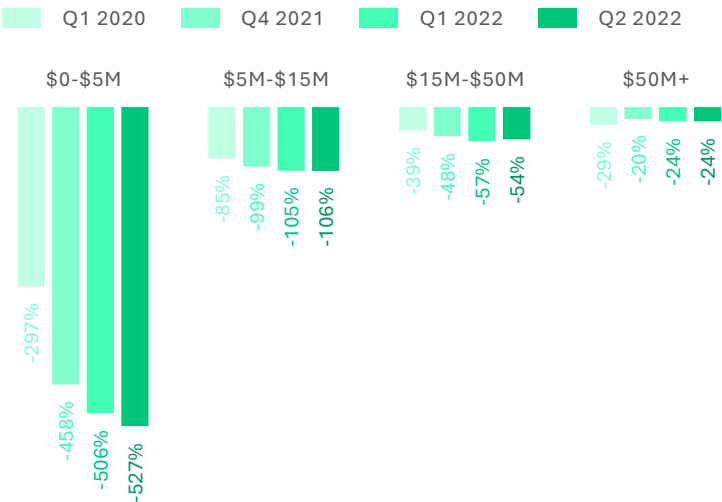
While spending was at near-record levels in Q1 2022, we are starting to see signs of companies cutting back. When we look at the aggregate payment volumes across select expense categories, we see that all are decreasing. The most significant decline is in ad spend, which is logical as companies can easily dial this back without disrupting business operations. It is far more difficult to cut payroll, but this activity has spiked recently, which is a similar story to public tech companies. Computing spend — specifically cloud computing spend — is also falling. This is notable as cloud computing spend tends to be a leading indicator of revenue changes as usage can be adapted quickly to demand. It should be noted that the impact from spending cuts to EBITDA is shrouded by one-time expenses, such as severance payments, which keep EBITDA margins flat.

Our findings mirror recent headlines. The Information’s subscriber survey¹ released in July 2022 reveals 38% of respondents are cutting marketing spend, 24% are cutting enterprise software budgets, 46% are slowing hiring or implementing hiring freezes, and 17% are making layoffs.

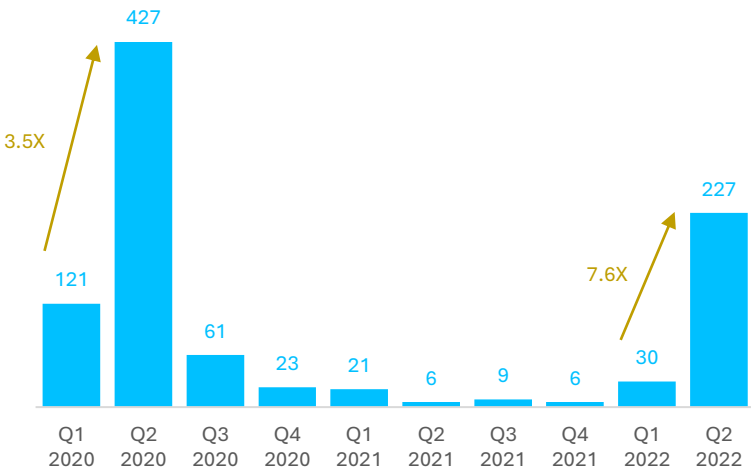
These measures generally mean a refocusing on the fundamentals of the business. It creates an opportunity for companies to focus on their core offerings and optimize workflows to achieve greater efficiencies. With the war on talent abating, companies have an opportunity to galvanize their workforce with top talent. Together, these dynamics mean companies can come out stronger.



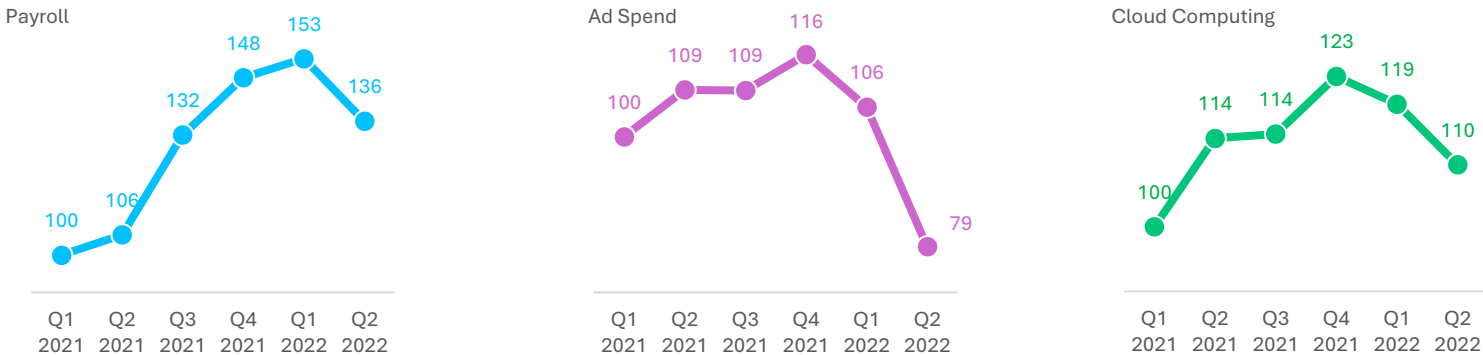
US VC-Backed Tech Companies Median EBITDA Margin by Annual Revenue Band²



Number of Tech Companies Reporting Layoffs



US VC-Backed Tech Companies Indexed Aggregate Spend by Select Categories³



Notable Vendors in Each Spend Category⁴



Notes: 1) 715 respondents, majority of respondents work at private companies, in tech finance or media, and identify as founders/executives. 2) Tech companies as defined by SVB’s proprietary taxonomy; annual revenue calculated by multiplying quarterly run rate by four. 3) Aggregate value of all transfers to merchants in the category indexed to 100 in Q1 2021. 4) Left to right: ADP, Gusto, TriNet, Facebook, Google, Twitter, Amazon Web Services, Google Cloud and Datadog. Source: SVB proprietary data, The Information, Layoffs.fyi and SVB analysis.



Exits:

Please Hold While Valuations Settle



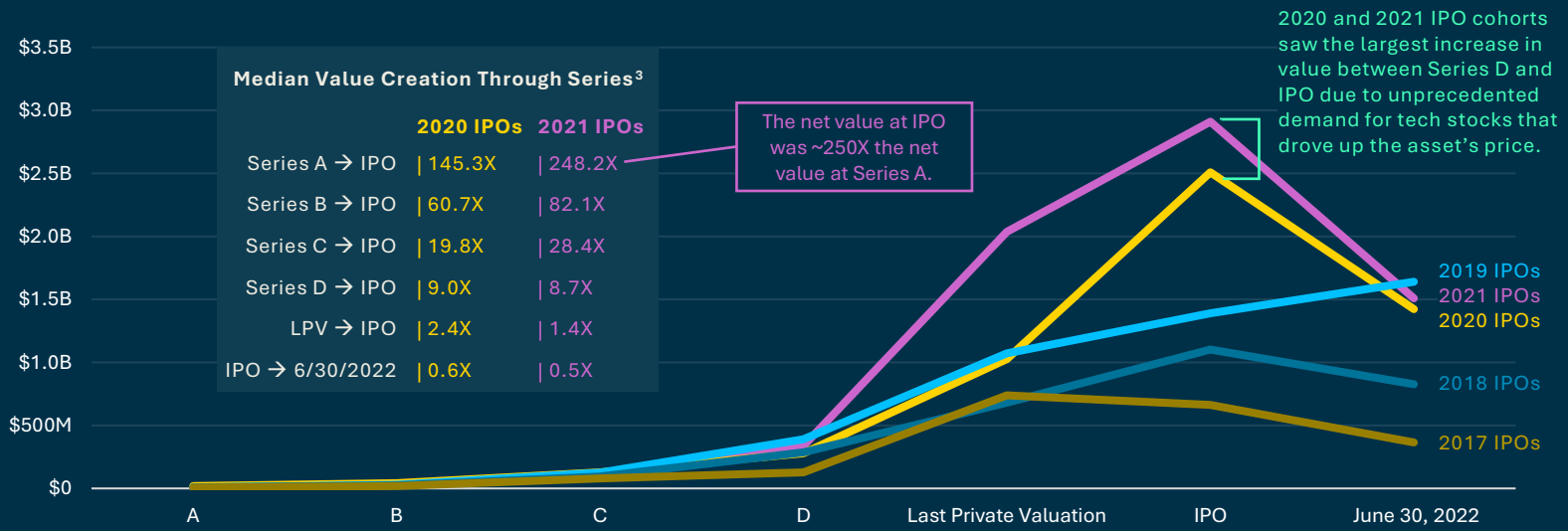
No-PO but Backlog Builds

The value of US VC-backed companies in recent years has surged. In the last five years, tech valuations at Series A and Series D have increased by \$28M and \$972M, respectively, but nowhere has the surge in valuations been more pronounced than at IPO. The median IPO valuation has increased by \$2.5B over the last five years.

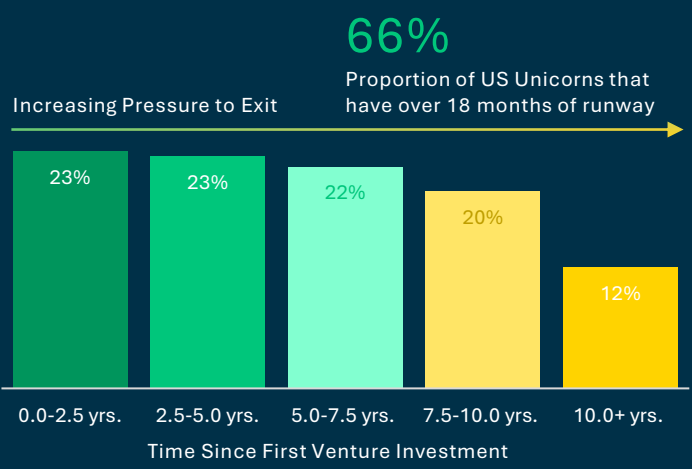
Macroeconomic uncertainty has led public market investors to rationalize valuations. In turn this has caused leadership teams to reevaluate their exit timelines. For example, JustWorks withdrew its IPO filing on July 13. As a result, only two US VC-backed tech IPOs occurred in H1 2022 — a 91% decrease compared to H1 2021.

When things do settle down, a significant stable of US unicorns created by the 2021 surge in late-stage capital will be ready. As of the end of Q2 2022, the aggregate value of US unicorns was approximately \$2.3T, based on their last private-round valuation. The median unicorn today has \$108M in annual revenue compared to just \$18M for IPOs during the dot-com bubble. This shows that today’s cohort is more established and probably better prepared for what lies ahead. When public markets do reopen, we expect a flurry of activity at favorable prices.

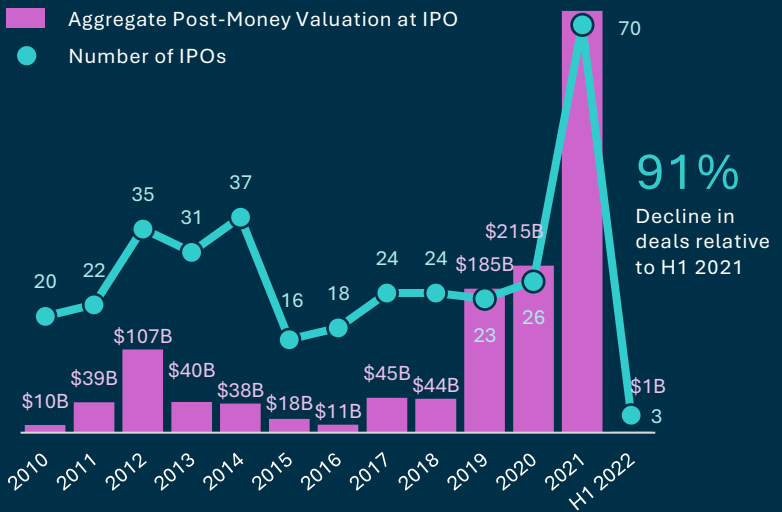
Median Value Created¹ by Stage for Prior US VC-Backed Tech IPO Cohorts²



Distribution of US Unicorn Value by Time Since First Venture Round⁴



US VC-Backed Tech IPOs by Year



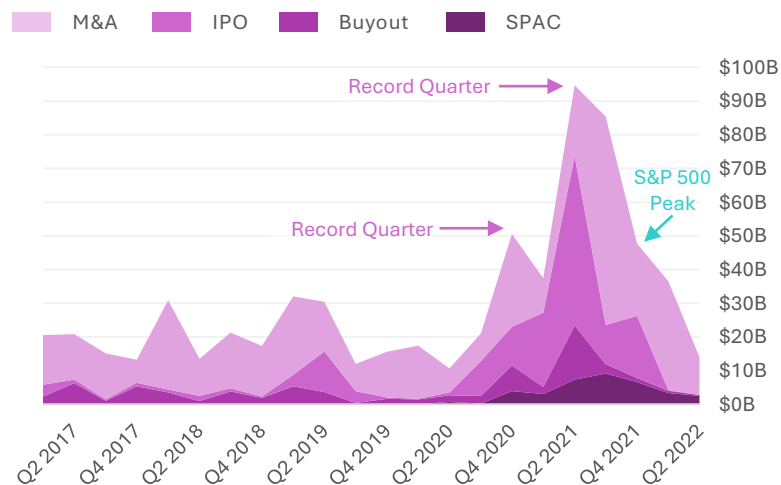
Notes: 1) Pre-money valuation (or market cap in the case of IPOs) net of all equity raised to date. 2) IPO on major US exchange. 3) Median value created for a stage divided by median value created by IPO; median value created calculated as pre-money valuation for the round less equity raised in all prior periods. 4) Unicorn data provided by PitchBook; includes US VC-backed companies that have reached and maintained at least a \$1B post-money valuation.
Source: PitchBook, S&P Capital IQ and SVB analysis.

Exit-Ready Companies Waiting for Their Opportunity

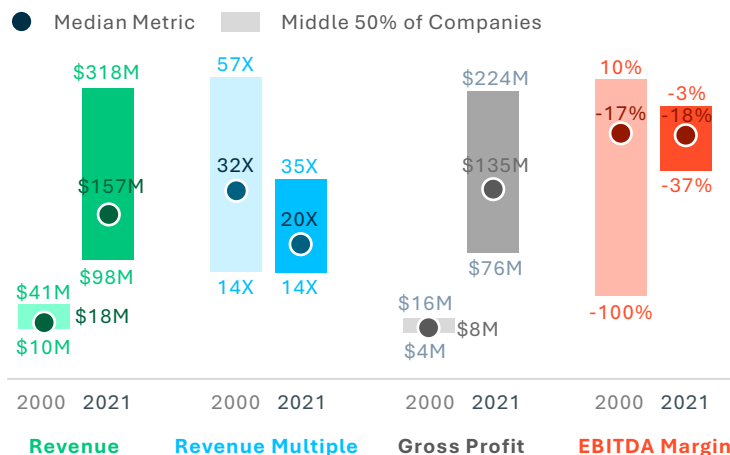
The hottest exit market in history — 70 VC-backed companies went public on a major US exchange in 2021 — closed in 2022, in large part due to the public market sell-off. For companies that went public in 2021 the median decline in valuation was 56%.¹ In addition to lackluster pricing, the volatility index (VIX) is still 38%² above the market peak on January 3, suggesting that IPO activity will remain muted since companies require a certain level of price certainty to plan and execute an exit. Although the IPO window is closed, the caliber of companies that went public in 2021 is far higher than those of the dot-com bubble (and subsequent crash). The vast majority have significantly more revenue and are priced much more reasonably (based on revenue multiple). Not surprisingly, profitability is also much healthier, although absolute cash burn is greater. EBITDA margins are poorer due to the (prior) growth-at-all-costs mantra touted by the innovation economy. For late-stage companies growing at over 50% a year, the median revenue multiple was 19X in 2021, while those growing at less than 50% had a multiple of 11X.³

Public market tumult is also suppressing SPAC merger activity, which is down 50% since Q2 2021. There are 587 SPACs currently looking for an acquisition target, 45% of which will expire within 12 months. For context, there were 184 closed mergers for the trailing 12 months, but this includes a record Q3 2021. Based on 2022's current merger rate, approximately 100 closed deals would be more probable.

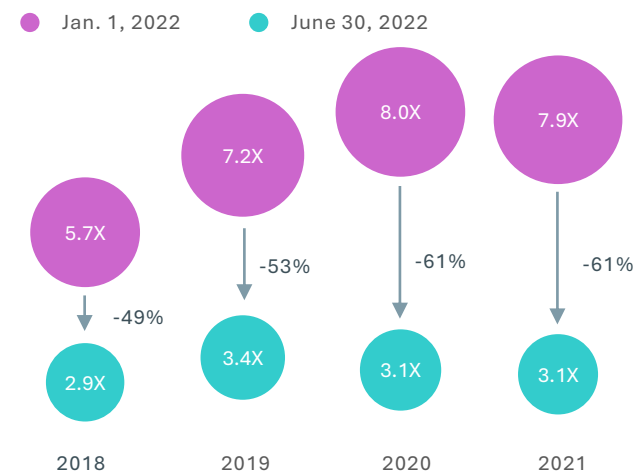
Aggregate Value of US VC-Backed Exits by Type (Excluding Healthcare)⁴



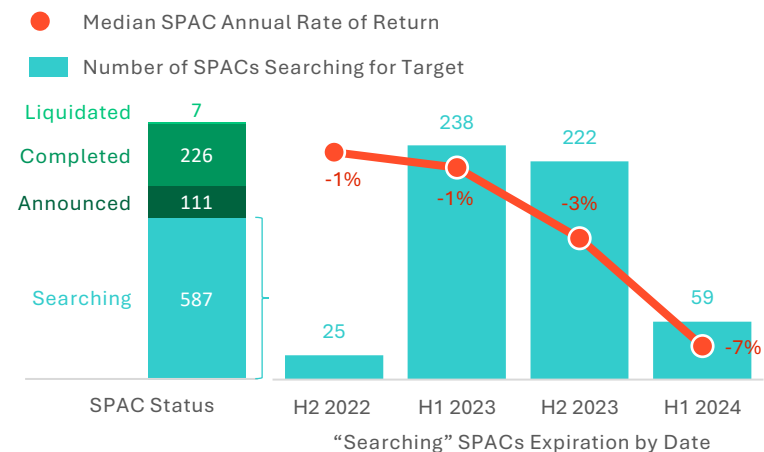
US VC-Backed Tech IPOs: Key Financial Metrics 2000 vs. 2021⁶



2021 US VC-Backed Tech IPOs: EV/NTM Revenue Multiple by Exit Year⁵



2020-2022 US SPAC Cohort Status, Expiration Schedule and Annual Rate of Return⁷



Notes: 1) Post-money IPO valuation to market cap on June 30, 2022. 2) As of August 1st, 2022. 3) For US, VC-backed tech companies with \$15M-\$35M in revenue. 4) Public exits on major US exchanges; value defined as post-money valuation. 5) US VC-backed tech IPOs on major US exchanges. 6) US, VC-backed information technology IPOs on any exchange; using PitchBook-NVCA Venture Monitor Search Criteria for IPOs. 7) Assumes 24 months from IPO to expiration. Cohort IPO years since 2020; assumes 24-month period to find a target.

Source: PitchBook, S&P Capital IQ, SPACInsider and SVB analysis.

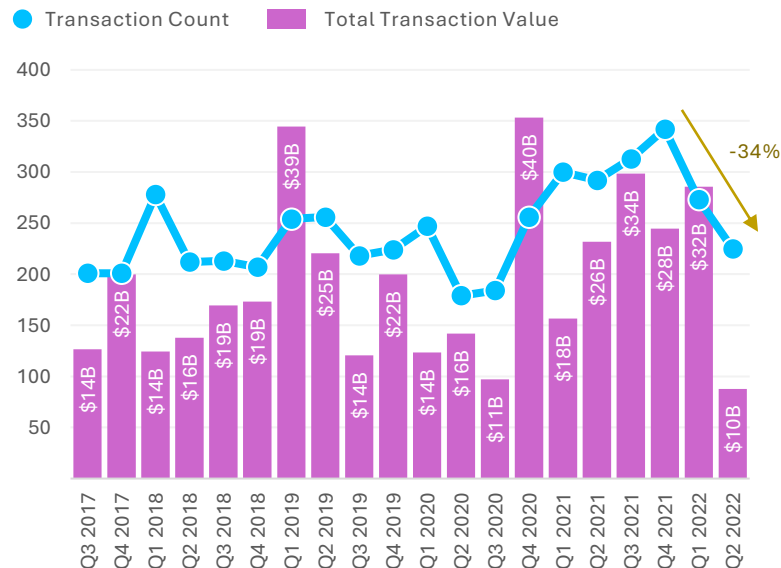
Buyers Wait for Lower Prices

The US VC-backed M&A market witnessed a robust period of activity starting in Q4 2020. Three out of the next five quarters were high-water marks for the number of M&A deals closed. Yet as with IPO activity, the narrative changed in 2022 as deal-making began to slow in response to tightening public markets. The slowdown so far has been most pronounced at the late-stage with the number of deals over \$100M decreasing 43% YoY. The sentiment of potential buyers is one of patience as they wait for prices to rebase.

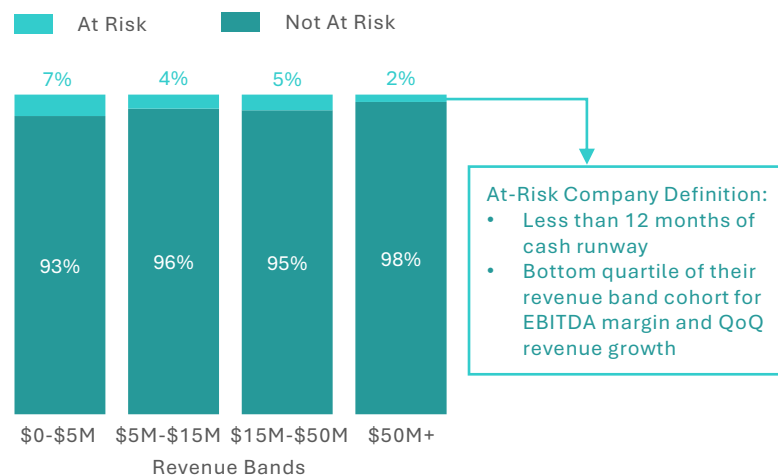
Market downturns stress company financials and make fundraising more difficult, leading some to seek opportunities through acquisitions. In 2021 acquirer “interest,” as gleaned by acquisition lines of credit issued, was elevated, but has since tapered off to more normalized levels in 2022. While there are inevitably startups that fail — in all market conditions — the stresses of downturns often cause failure rates to increase. However, the durability of the innovation economy is much greater than in the past, with a relatively small fraction of companies “at risk.”

Ultimately, downturns offer an opportunity for many companies to consolidate market share. Acquisitions offer the opportunity to consolidate technology and talent. Coupled with the efficiency gains from cutting expenses and focusing on the core, many companies will be stronger on the other side.

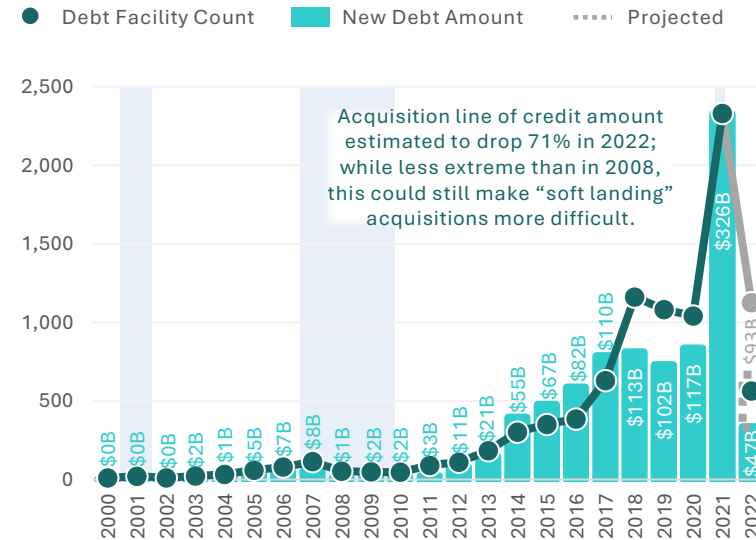
US VC-Backed M&A Activity



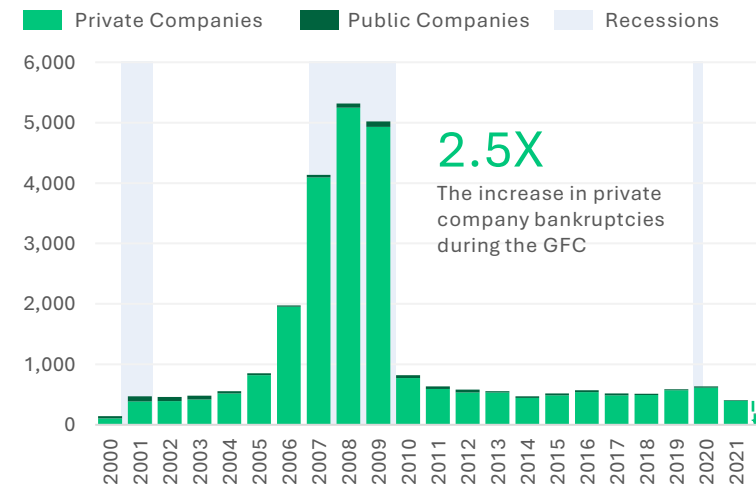
Distribution of At Risk US, VC-Backed Tech Companies by Revenue Band³



Acquisition Lines of Credit Issued in the US²



Bankruptcies of US-Based Companies⁴



Notes: 1) Data based on M&A announcement date; only M&As with a non-zero transaction value are included; data for 2022 is interpolated based on numbers as of 7/7/2022. 2) Data includes acquisition financing deals that were completed by companies located in the US; 2022 data is interpolated based on H1 numbers. 3) US VC-backed private tech companies with negative EBITDA margins using Q2 2022 financial statements. 4) Data for 2022 is interpolated based on H1 numbers and is denoted “2022E.”

Source: S&P Capital IQ, PitchBook, Mergermarket, SVB proprietary data and SVB analysis.



International:

Global Perspectives



A Soaring Dollar Extends Runway

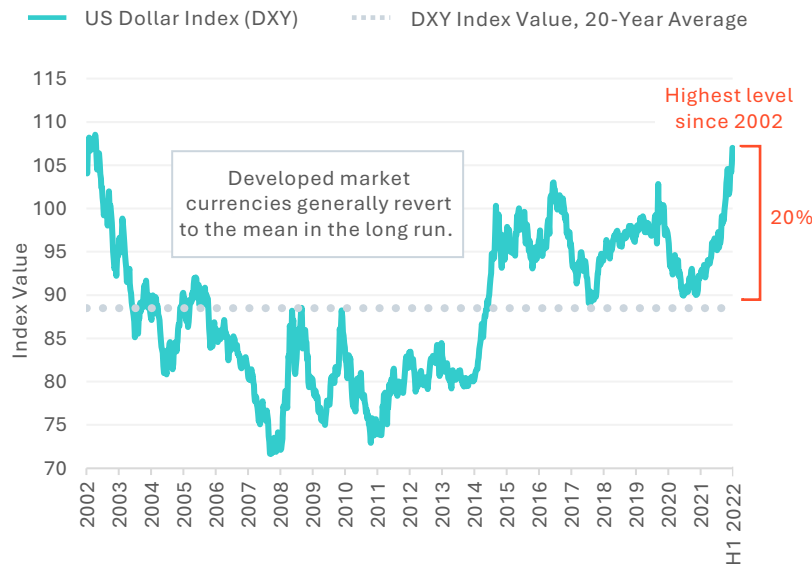
The US dollar (USD) is trading near a 20-year high relative to other significant (by trade volume) currencies. The current volatile geopolitical climate centered in Europe is putting downward pressure on the euro. Conversely, rising rates in the US and global public market volatility are driving investors to “safe” assets such as US T-bills. The USD has rallied, reaching parity with the euro on July 11.

The narrative from news headlines and earnings reports typically emphasizes how a strong dollar negatively impacts big tech, but for cash-burning private tech companies a strong dollar is a boon. The currency exposure of big tech companies skews toward being a net buyer of dollars, due to the repatriation of foreign currency revenues. This differs for the vast majority of US-based private tech companies, as they are net sellers of USD by a 3:1 margin. So, a strong dollar leads to improved EBITDA for 73% of US tech companies that are net sellers of the dollar and, in turn, extends cash runway.

Companies with a larger net long USD position (net seller) relative to their revenue saw the most significant gains in their profitability and cash runway, both of which are beneficial given that the equity fundraising environment has become more challenging. However, these companies are equally exposed to the downside of foreign exchange (FX) volatility. Just as they have experienced a 5%-10% increase in runway due to positive FX movements, these companies could similarly experience the same decline if the USD were to reverse. This underlines the importance of a dynamic hedging strategy.

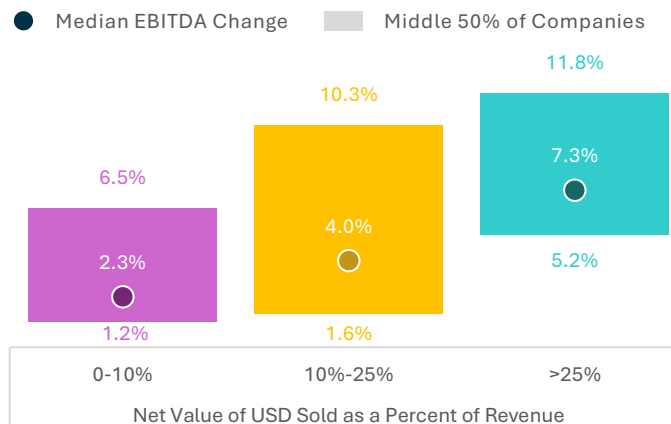


USD Dollar Index¹

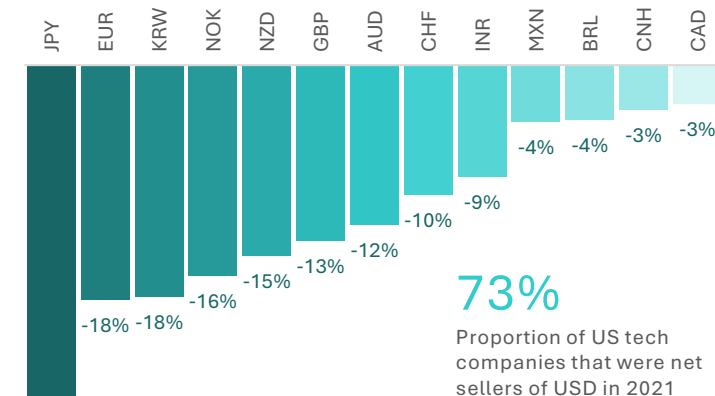


US VC-Backed Tech: FX Effects on EBITDA³

Percent change in company EBITDA resulting from the USD rally over the last 18 months:

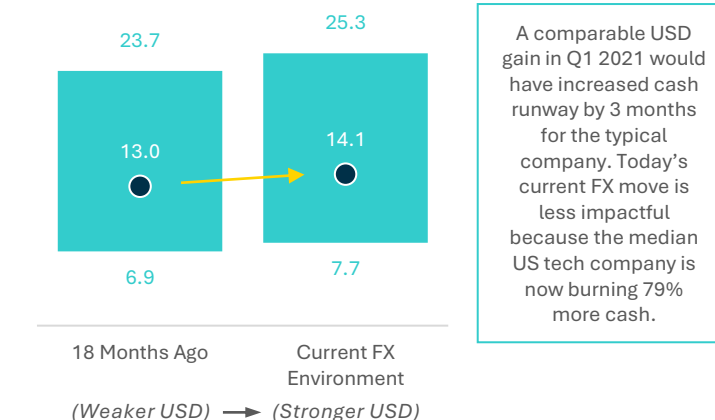


Select Currency Changes vs. USD During Current USD Bull Run²



US VC-Backed Tech: FX Effects on Cash Runway (in Months)^{3,4}

● Median Runway Change ■ Middle 50% of Companies



Notes: 1) The USD Index is an index of the value of the United States dollar relative to a basket of foreign currencies, often referred to as a basket of US trade partners' currencies. 2) From 1/1/2021 to 7/14/2022. 3) For US tech companies with negative EBITDA that have at least a \$2M net short position on the USD; analysis based on change in DXY index 1/1/2021 to 7/14/2022. 4) For companies with at least \$5M in revenue. Source: SVB proprietary data, Bloomberg and SVB analysis.

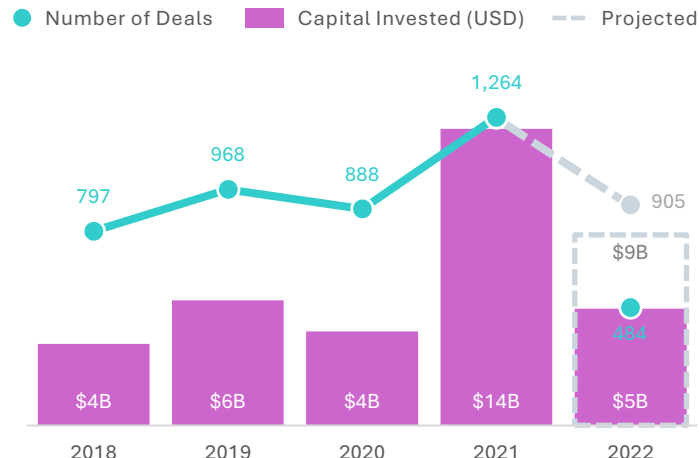
In Canada Cooler Heads Prevail

The Canadian innovation economy has been growing, epitomized by a 42% increase in deal activity in 2021. Deals are also getting larger. In 2020 there were just two deals over \$100M. In 2021, this number jumped to 35 and, even with a tumultuous 2022, 14 deals over \$100M had closed by H1. As with the US ecosystem, companies have increased their cash reserves in response to increased uncertainty from the COVID-19 pandemic, capitalizing on a robust fundraising environment that offered “cheap” (less dilution due to rising valuations) equity capital.

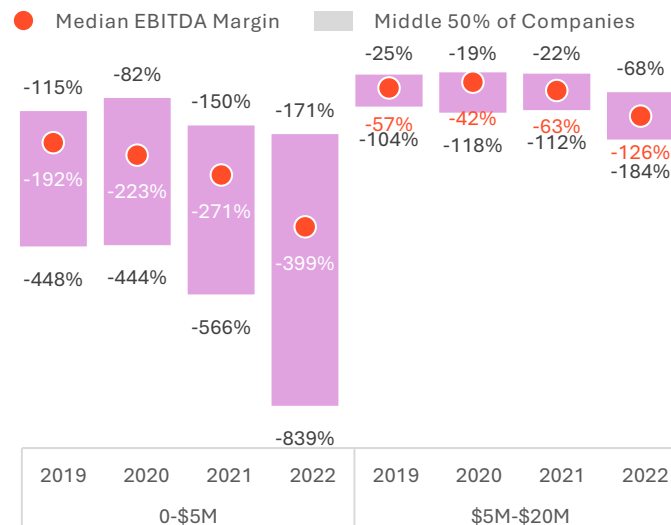
At the same time that companies were increasing cash, they were also increasing their burn. EBITDA margins became increasingly negative, ignoring a brief cost-cutting period at the start of the pandemic. Given companies could relatively “easily” raise more equity, profitability fell to the wayside in favor of growth. Companies, with their larger cash reserves, could be well positioned to weather an extended downturn, providing they are able to quickly cut spend to reduce burn. Canadian companies have a long standing reputation for being capital-efficient relative to their US and international counterparts. On the ground, we are seeing companies react. This will be essential to Canadian companies, as investors take a pause and the power dynamic swings from founders back to investors. We expect to see significant improvement in EBITDA margins over the next four quarters, as companies react to extend runway in preparation for an extended downturn.



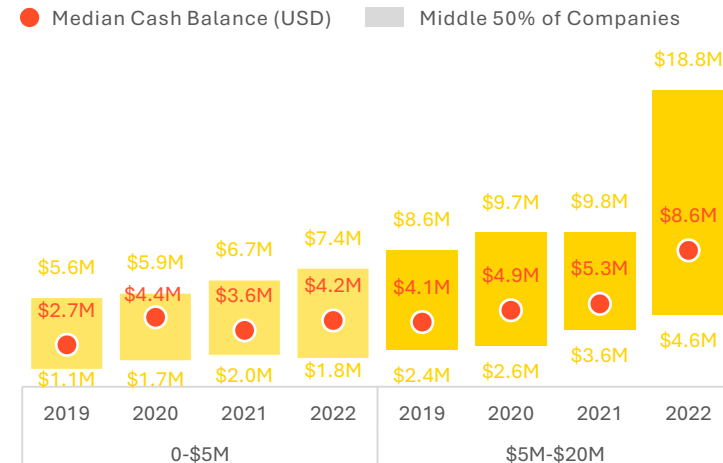
Canadian VC Investment



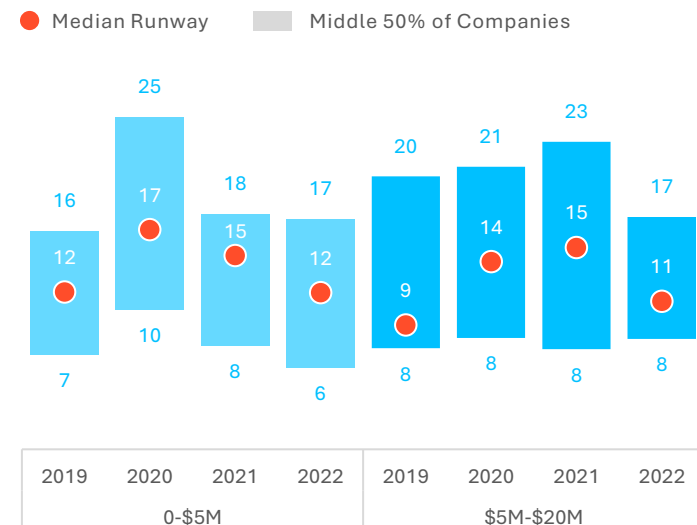
VC-Backed Canadian Tech: EBITDA Margin by Annual Revenue (USD) Band¹



VC-Backed Canadian Tech: Cash Balance by Annual Revenue (USD) Band¹



VC-Backed Canadian Tech: Cash Runway in Months by Annual Revenue (USD) Band^{1,2}



Notes: 1) Tech companies as defined by SVB's proprietary taxonomy; annual revenue calculated using quarterly run rate and multiplying by four. 2) For negative cash flow companies.
Source: PitchBook, SVB proprietary data and SVB analysis.

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