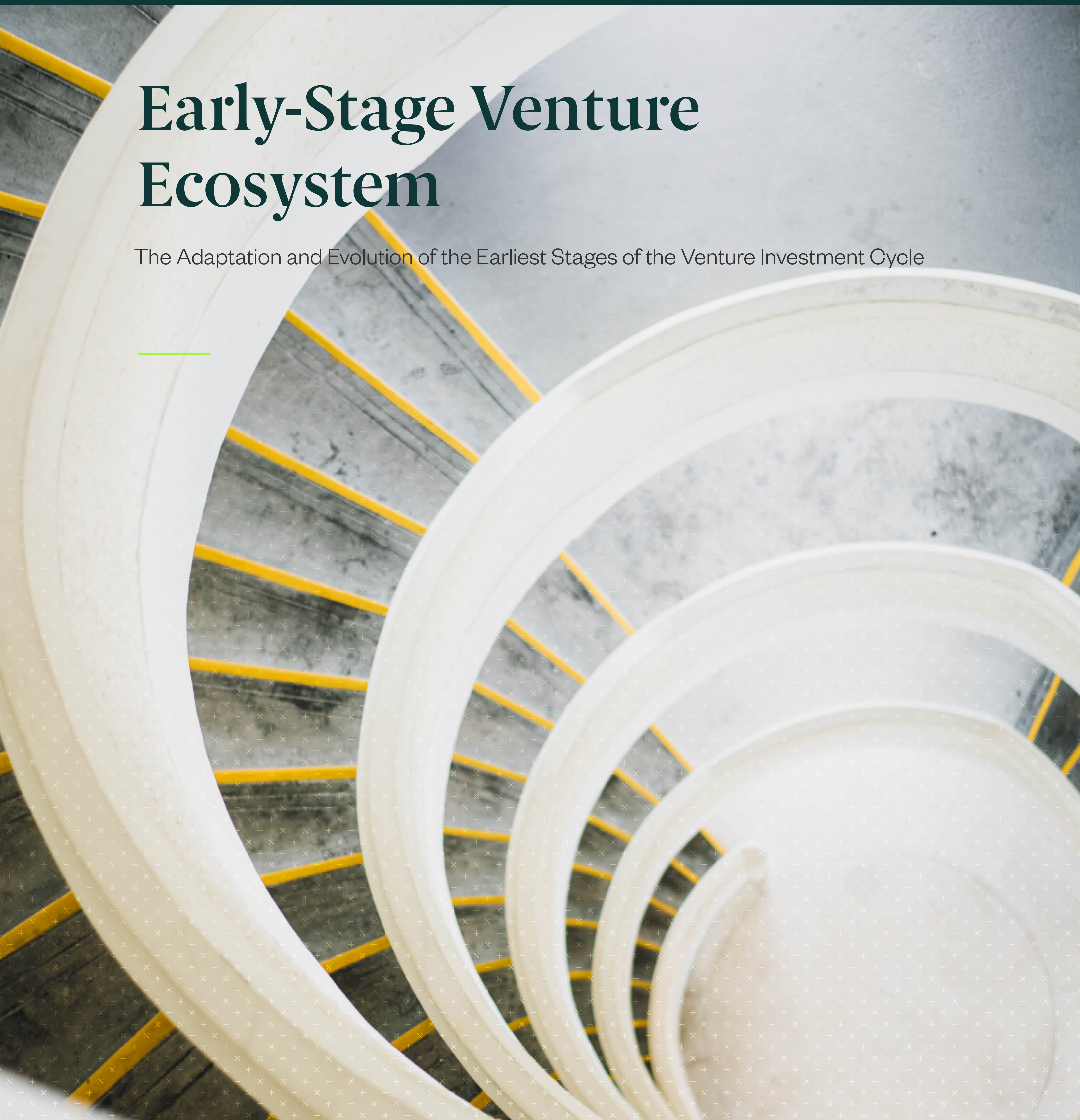
MOSSADAMS

Early-Stage Venture Ecosystem

The Adaptation and Evolution of the Earliest Stages of the Venture Investment Cycle



CONTENTS

INTRODUCTION

Tailwinds continue to be strong for the early- and growth-stage investment environment.

This is fueled by an endless supply of innovation and transformation that's happening at a more rapid rate across all industries in addition to increased capital resources looking to be deployed. Traditional industry lines are blurred by technology, which is appealing to investors and innovators as increased opportunity.

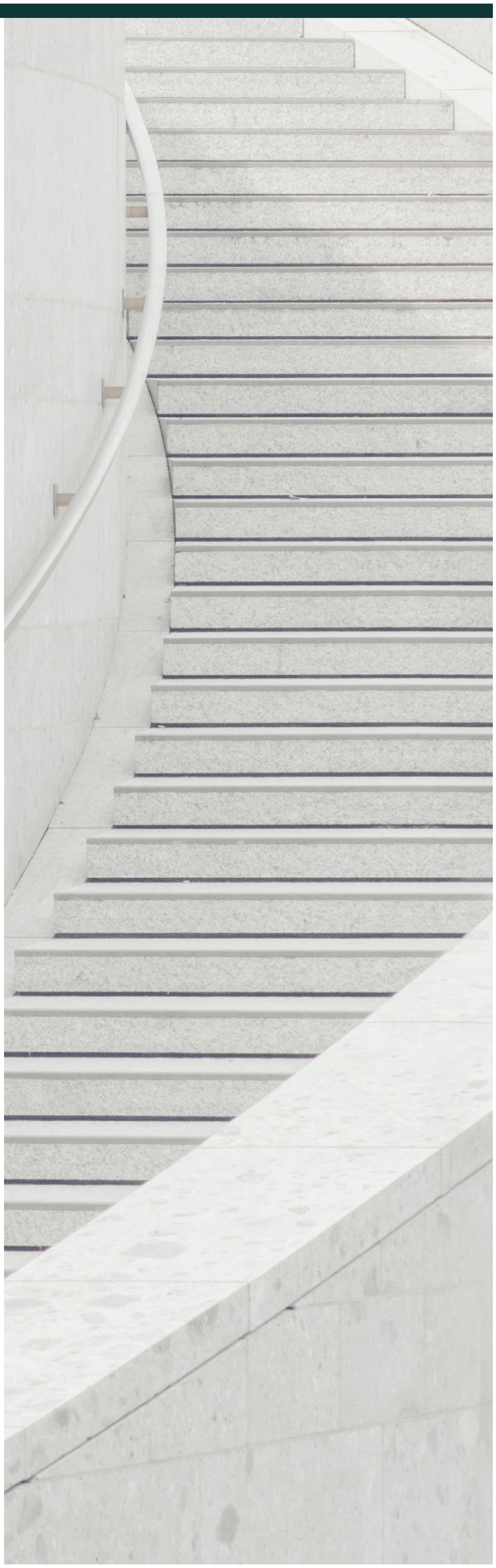
Investors and investment models have matured over the past 25 years, making the innovation ecosystem more efficient and effective.

Below is a quick look at what the early-stage venture ecosystem looks like. We hope you find this report useful.

- TAFT KORTUS, NATIONAL INDUSTRY GROUP LEADER
TECHNOLOGY, COMMUNICATIONS & MEDIA,
AND LIFE SCIENCES PRACTICES

EARLY-STAGE VENTURE ECOSYSTEM AT A GLANCE

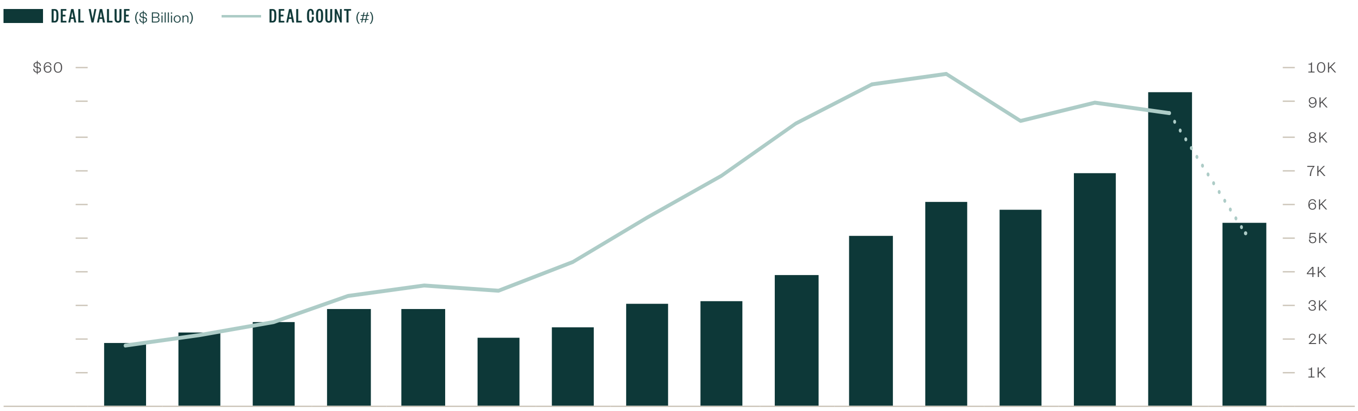
- The year 2018 sees record $50.1 billion invested across close to 8,000 transactions at the early stage.
- Median early-stage financing sizes across nearly all stock types hit new highs in 2019 to date.
- In tandem, median pre-money valuations climb to record highs across seed, Series A, and Series B financings, with Series B financings experiencing significant rates of increase.
- Pharma and biotech start-ups rake in no less than $6.2 billion of early-stage funding in 2019 to date and software stays on track.
- Early-stage deal making is globalizing. Foreign investor participation hits a new high in deal value in 2018 while activity remains robust.
- Even at the early stage, exits have been historically high, with 2019 notching $11.6 billion in aggregate value across 259 transactions.
- Fundraising amid early-stage size ranges is still strong but in cyclical diminution as market conditions evolve.



EARLY-STAGE DEAL MAKING

The US venture ecosystem is flush with capital. Institutional investors' allocations to alternative investments have grown in the past decade and fundraising has consistently posted strong figures for years.

FIGURE 1: Early-Stage Venture Capital (VC) Activity: Deal Value and Deal Count
United States, 2004–2019 YTD, ($ Billion)



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019*
Value	$9.9	$11.6	$13.6	$15.6	$15.6	$10.8	$12.4	$16.1	$16.9	$20.7	$27.1	$32.5	$31.1	$37.0	$50.1	$29.1
Count	1,625	1,918	2,214	2,904	3,182	3,059	3,821	5,036	6,112	7,473	8,560	8,849	7,600	8,025	7,791	4,581

* As of August 6, 2019

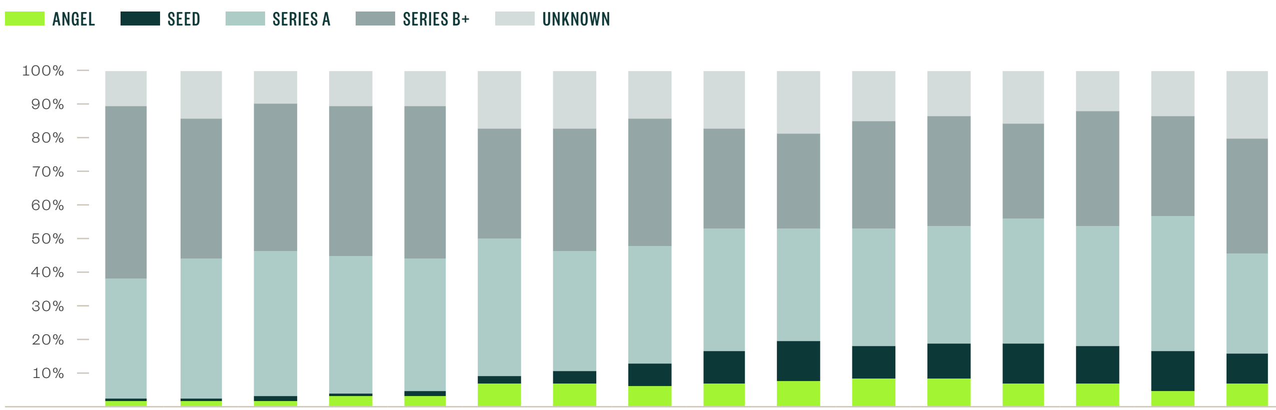
This expansion and inflation at the late stage has exerted ripple effects across the entire venture cycle, particularly at the early stage.

It's led to new fund formation but also to significant growth on the part of flagship venture firms, which can now close on multibillion-dollar vehicles. Moreover, nontraditional investors completely transformed the late to growth stages of the venture landscape and contributed to the proliferation of once-rare unicorns.

> "Seed and pre-seed rounds have grown larger and carried companies to a much later stage than in previous years. This has inherently caused seed investors to become more knowledgeable about their portfolio companies and the markets in which they operate."
>
> – CHERYL TEETER-BALIN, PARTNER, ASSURANCE SERVICES

Early-Stage VC Activity: Percentage Deal Value by Stock Type

United States, 2004–2019 YTD, ($ Billion)

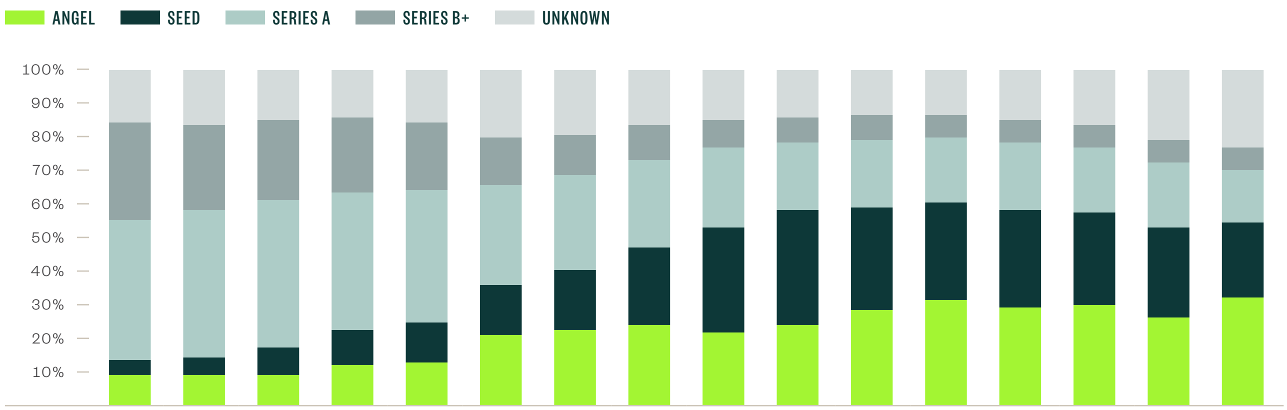


	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019*
Angel	$0.2	$0.2	$0.2	$0.4	$0.4	$0.7	$0.8	$1.0	$1.1	$1.5	$2.2	$2.8	$2.1	$2.5	$2.3	$2.0
Seed	$0.1	$0.1	$0.2	$0.2	$0.3	$0.3	$0.4	$1.1	$1.7	$2.4	$2.5	$3.3	$3.6	$4.2	$5.9	$2.5
Series A	$3.5	$4.9	$5.9	$6.3	$6.2	$4.4	$4.5	$5.7	$6.2	$7.0	$9.6	$11.3	$11.8	$13.2	$20.4	$8.8
Series B+	$5.1	$4.8	$5.9	$7.0	$7.1	$3.6	$4.5	$6.1	$5.0	$5.8	$8.7	$10.7	$8.7	$12.9	$14.8	$10.0
Unknown	$1.1	$1.7	$1.3	$1.7	$1.7	$1.8	$2.1	$2.3	$2.9	$3.9	$4.0	$4.4	$5.0	$4.3	$6.8	$5.8

* As of August 6, 2019

FIGURE 2: Early-Stage VC Activity: Percentage Deal Count by Stock Type

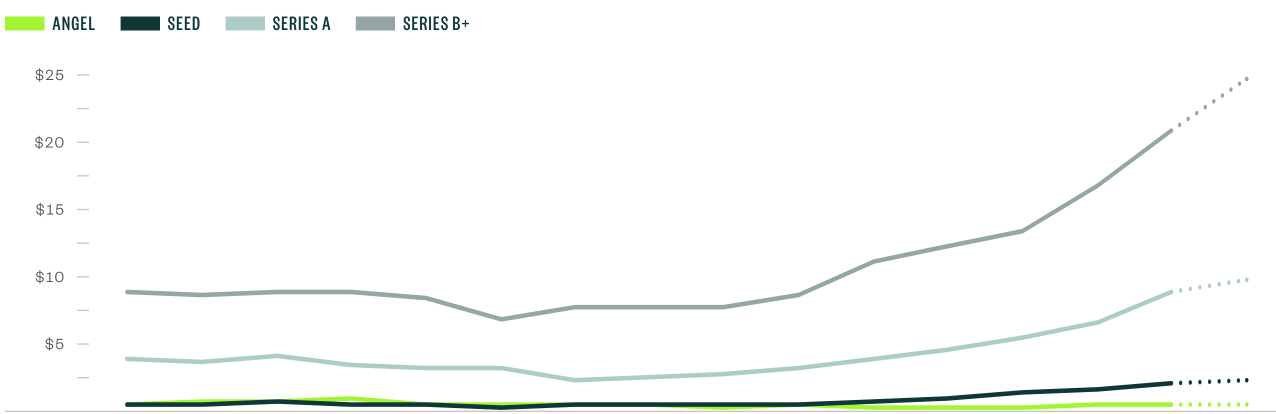
United States, 2004–2019 YTD



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019*
Angel	143	165	201	346	397	640	850	1,185	1,314	1,786	2,397	2,793	2,186	2,363	2,039	1,450
Seed	78	108	178	299	384	458	697	1,188	1,928	2,526	2,630	2,567	2,216	2,213	2,102	1,055
Series A	675	836	969	1,191	1,250	914	1,084	1,298	1,425	1,526	1,742	1,695	1,543	1,562	1,458	702
Series B+	468	491	530	647	655	424	448	537	507	536	616	621	533	546	576	297
Unknown	261	318	336	421	496	623	742	828	938	1,099	1,175	1,173	1,122	1,341	1,616	1,077

Early-Stage VC Activity: Median Deal Size by Stock Type

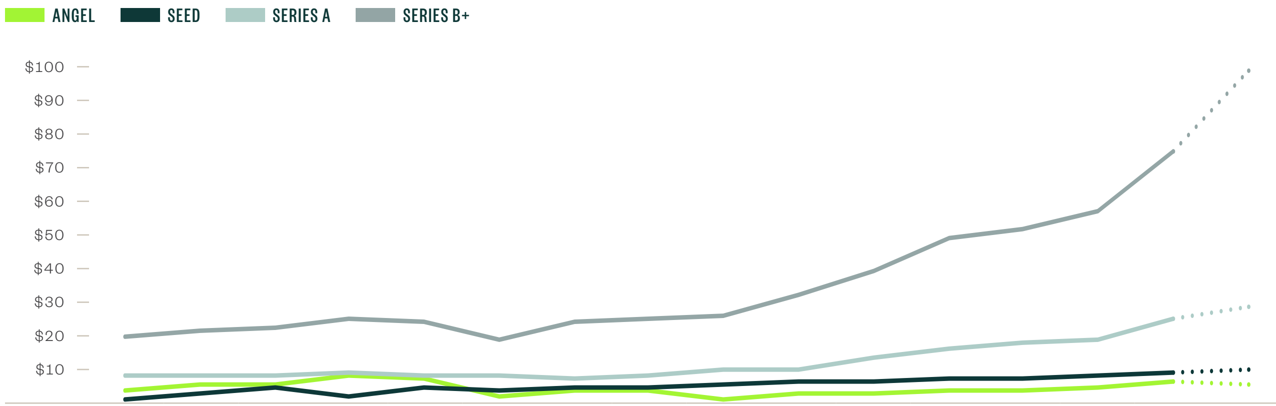
United States, 2004–2019 YTD, ($ Million)



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019*
Angel	$0.6	$0.8	$0.7	$0.9	$0.6	$0.5	$0.5	$0.4	$0.4	$0.4	$0.4	$0.4	$0.4	$0.5	$0.5	$0.6
Seed	$0.5	$0.5	$0.6	$0.5	$0.5	$0.4	$0.5	$0.5	$0.5	$0.6	$0.7	$1.0	$1.4	$1.6	$2.0	$2.1
Series A	$3.5	$3.2	$3.7	$3.0	$3.0	$2.9	$2.1	$2.3	$2.6	$3.0	$3.5	$4.1	$5.0	$6.0	$8.0	$8.8
Series B+	$8.0	$7.7	$8.0	$8.0	$7.6	$6.0	$7.0	$7.0	$6.9	$7.8	$10.0	$11.0	$12.0	$15.0	$18.5	$22.0
Angel	121	137	169	294	369	581	779	962	1,094	1,453	1,960	2,415	2,021	2,236	1,960	1,412
Seed	58	81	137	219	296	358	567	1,004	1,656	2,227	2,279	2,204	1,936	1,977	1,841	897
Series A	662	817	948	1,164	1,220	892	1,048	1,263	1,386	1,476	1,667	1,637	1,492	1,496	1,390	678
Series B+	462	488	522	638	646	415	436	526	495	515	605	606	519	539	562	287

* As of August 6, 2019

FIGURE 3: Early-Stage VC Activity: Median Pre-Money Valuation by Stock Type
United States, 2011–2019 YTD, ($ Million)



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019*
Angel	$3.0	$4.0	$4.0	$6.3	$5.4	$1.1	$2.5	$3.0	$0.9	$2.1	$1.8	$2.9	$2.5	$3.6	$4.8	$4.4
Seed	$0.8	$2.2	$3.3	$1.5	$3.7	$2.9	$3.2	$3.8	$4.0	$4.6	$4.9	$5.3	$5.7	$6.3	$7.0	$7.7
Series A	$6.0	$6.4	$6.6	$6.9	$6.5	$6.0	$5.7	$6.7	$7.5	$8.0	$10.5	$12.6	$14.0	$15.0	$20.0	$23.0
Series B+	$16.0	$17.0	$18.1	$20.0	$19.0	$15.0	$19.0	$20.1	$20.6	$25.9	$31.5	$39.4	$41.9	$46.0	$60.0	$80.0
Angel	1	2	5	8	8	12	7	33	55	85	120	149	98	97	99	24
Seed	4	6	15	14	32	55	142	248	485	682	874	1,114	1,117	1,202	1,014	471
Series A	419	517	583	759	788	673	821	1,032	1,100	1,181	1,334	1,318	1,205	1,193	1,036	472
Series B+	266	299	334	406	430	292	337	425	411	443	523	510	434	430	459	202

* As of August 6, 2019

A record sum was invested in 2018 at the early stage, even while deal volume held steady. As seed financings saw their median size exceed $2 million in 2019 to date—with an accompanying valuation figure of more than $7 million—many industry pundits have hypothesized that traditional nomenclature is no longer valid; however, it has more likely evolved.

Traditional nomenclature has broken down only in the sense that the metrics of Series A financings are close to or exceeding what companies received in Series B funds in the early 2000s (post the dot-com era). It isn't that each deal type has seen its own inflation; rather, growth has forced companies and investors to evolve their strategies and approaches in tandem with growth in capital availability and dispensing.

This transformation has been most dramatic at the early stage.

"The VC market in general, and the seed market in particular, continue to evolve over time. There's a level of sophistication and precision in the way both investors and entrepreneurs approach the funding cycle, and it is constantly being adapted."

– GASSEN MOSBAHI, PARTNER, TRANSACTION SERVICES

An illustrative example is the slight diminution in angel financing volume since its peak in 2015. Whereas seed financing volume has held steady in its proportion of overall deal flow, angel volume decreased and has since held somewhat steady.

Because angel financing is the riskiest segment of the VC stack, a decline as relative financing sizes grew isn't uncommon. However, seed and even Series A's resilience is attributable to the ability of VC investors to develop more specific niche strategies due to companies at this stage generally having more traction—for example, more data to craft targeted investment theses.

Current businesses looking for seed funding are still nascent, often with just a key founding group, product idea, and target need. The intriguing conclusion from the profundity of seed-stage and all early-stage VC investment figures is that the ratio of capital to investment-worthy opportunities is still overly weighted in the numerator.

> "For the last three to five years it seemed like a new VC fund was formed almost daily. In the long term, not all will be successful, but the perceived opportunity and ease of raising capital invited many to join the table. Now we are seeing a significant amount of dry powder from these newly formed VC funds with insufficient portfolio companies to deploy."

– CHERYL TEETER-BALIN

Some of that lopsidedness is due to sheer cost levels inducing caution on the part of VCs, hence deal making holding relatively steady across early-stage proportions instead of surging even further. Growth in valuations is also somewhat correcting of excessive volume. VC firms are urging greater deliberation and clearer pathways to business milestones.

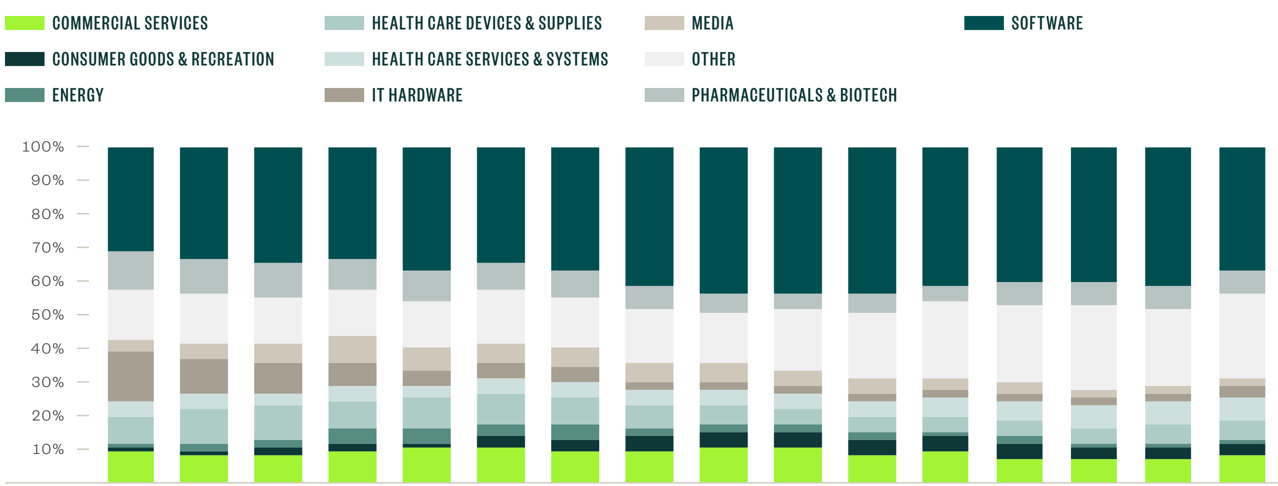
> "Investors are putting more emphasis on revenue growth, quality and momentum. There has been more recent attention given to management's ability to take available cash funds further. Investors want to make sure management allocates the available cash properly and efficiently and does not go on a spending spree that will push the company to go out and try to raise more money."

– GASSEN MOSBAHI

Especially in the current early-stage market, investors are allocating more focus and capital to B2B models as well as health care and cybersecurity. They are diverting attention from consumer-driven start-ups that may bear excessive exposure to economic concerns that typically crop up late in economic and market cycles.

FIGURE 4: Early-Stage VC Activity: Percentage Deal Count by Sector

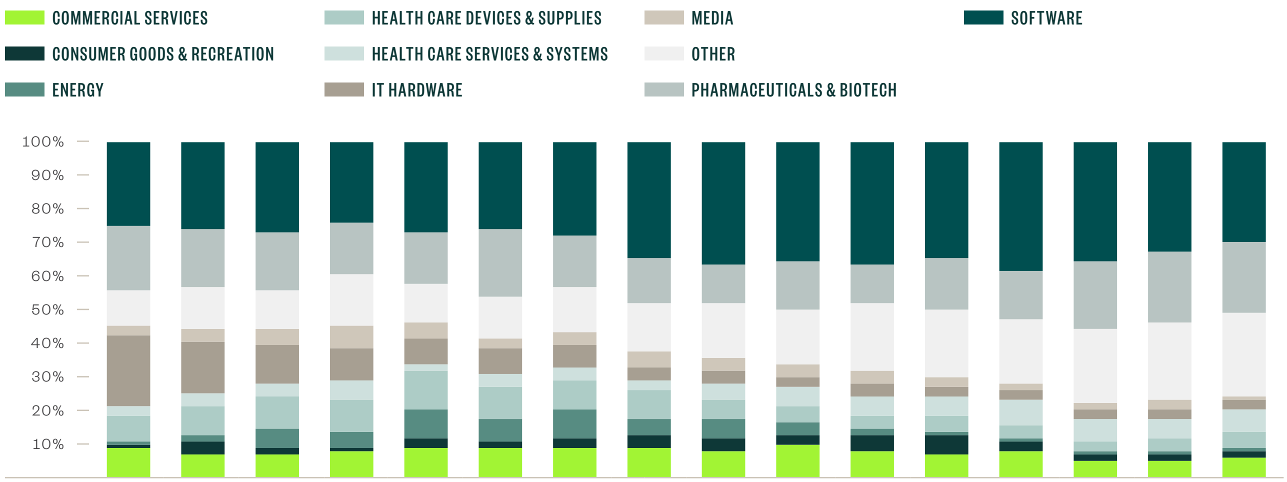
United States, 2004–2019 YTD



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019*
	146	157	172	281	312	315	372	471	629	783	734	765	567	546	561	345
	23	27	49	56	70	91	133	200	261	331	367	407	324	274	269	179
	21	33	60	115	132	119	163	133	139	141	142	136	126	96	93	60
	135	192	232	260	281	291	296	333	370	364	389	429	373	413	409	255
	67	91	76	117	112	147	187	234	278	369	403	465	456	476	519	340
	253	212	203	197	149	144	150	145	147	177	204	195	163	206	198	124
	47	82	130	237	216	172	234	303	376	352	421	340	235	216	161	102
	246	299	309	414	450	473	577	790	934	1,316	1,705	2,044	1,820	2,069	1,808	1,170
	187	189	219	268	283	260	322	328	331	391	422	460	448	550	554	353
	500	636	764	959	1,177	1,047	1,387	2,099	2,647	3,249	3,773	3,608	3,088	3,179	3,219	1,653

* As of August 6, 2019

FIGURE 5: Early-Stage VC Activity: Percentage Deal Value by Sector
United States, 2004–2019 YTD, ($ Billion)



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019*
	$0.8	$0.8	$0.8	$1.1	$1.3	$0.9	$1.1	$1.3	$1.2	$1.9	$2.1	$2.2	$2.2	$1.5	$2.1	$1.5
	$0.1	$0.4	$0.2	$0.2	$0.4	$0.2	$0.3	$0.7	$0.7	$0.7	$1.1	$1.7	$1.0	$0.7	$1.2	$0.7
	$0.1	$0.2	$0.8	$0.8	$1.5	$0.7	$1.1	$0.8	$0.9	$0.8	$0.5	$0.5	$0.3	$0.4	$0.5	$0.4
	$0.7	$1.1	$1.4	$1.5	$1.7	$1.1	$1.1	$1.3	$1.1	$1.0	$1.2	$1.4	$1.1	$1.3	$2.1	$1.4
	$0.3	$0.4	$0.5	$0.9	$0.4	$0.4	$0.5	$0.5	$0.7	$1.1	$1.6	$1.9	$2.4	$2.3	$2.8	$1.8
	$2.1	$1.8	$1.6	$1.5	$1.1	$0.8	$0.8	$0.6	$0.8	$0.6	$0.8	$1.0	$1.0	$1.1	$1.2	$0.8
	$0.3	$0.4	$0.6	$1.1	$0.8	$0.3	$0.5	$0.6	$0.6	$0.8	$1.0	$0.8	$0.6	$0.7	$1.5	$0.3
	$1.1	$1.5	$1.6	$2.4	$1.8	$1.4	$1.7	$2.4	$2.6	$3.4	$5.6	$6.8	$6.0	$8.2	$11.8	$7.4
	$1.9	$2.0	$2.3	$2.4	$2.4	$2.2	$2.0	$2.2	$2.0	$3.0	$3.0	$4.8	$4.6	$7.5	$10.4	$6.2
	$2.5	$3.0	$3.7	$3.8	$4.2	$2.8	$3.4	$5.5	$6.2	$7.5	$10.0	$11.4	$11.9	$13.1	$16.5	$8.7

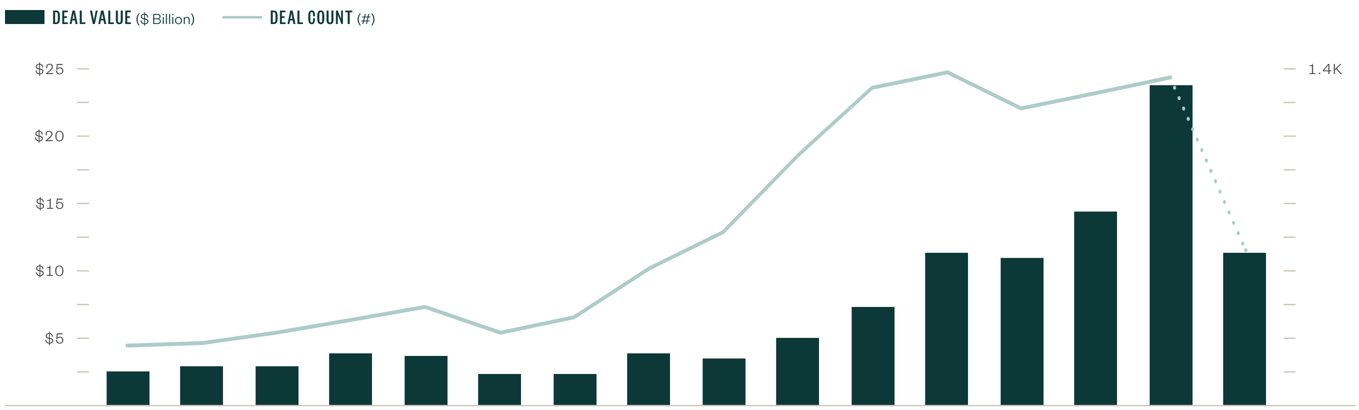
* As of August 6, 2019

The pharma and biotech sector stands out in terms of dollars invested in 2019 to date, clocking $6.2 billion as of early August. However, start-ups in such arenas can still close on funding, given the sheer accessibility and volume of capital in the market. They simply must prove out key factors in a more robust fashion, especially across the early stage—in short, proven monthly recurring revenue is highly attractive to investors.

> “If companies aren’t progressing with speed through the fundraising cycle at 18-month to two-year intervals, it can be increasingly difficult for them to source capital. Companies may also need to accept less-favorable terms to bring in capital or spend time to clean up their existing cap tables. The willingness to continue to fund still seems to exist, even in challenging conditions.”
>
> – CHERYL TEETER-BALIN

Finally, a defining characteristic of the changing early-stage ecosystem is increasing globalization. As can be seen from the accompanying PitchBook dataset, early-stage venture activity with foreign investor participation has persisted at a high level for years now, with a record sum of associated deal value in 2018.

FIGURE 6: Early-Stage VC Activity with Foreign Investor Participation: Deal Value and Deal Count United States, 2004–2019 YTD



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019*
Value	$2.3	$2.8	$2.7	$3.6	$3.5	$2.2	$2.2	$3.6	$3.3	$4.7	$6.9	$10.8	$10.4	$13.6	$22.7	$10.7
Count	236	251	288	338	390	285	345	538	690	991	1,256	1,318	1,172	1,237	1,302	619

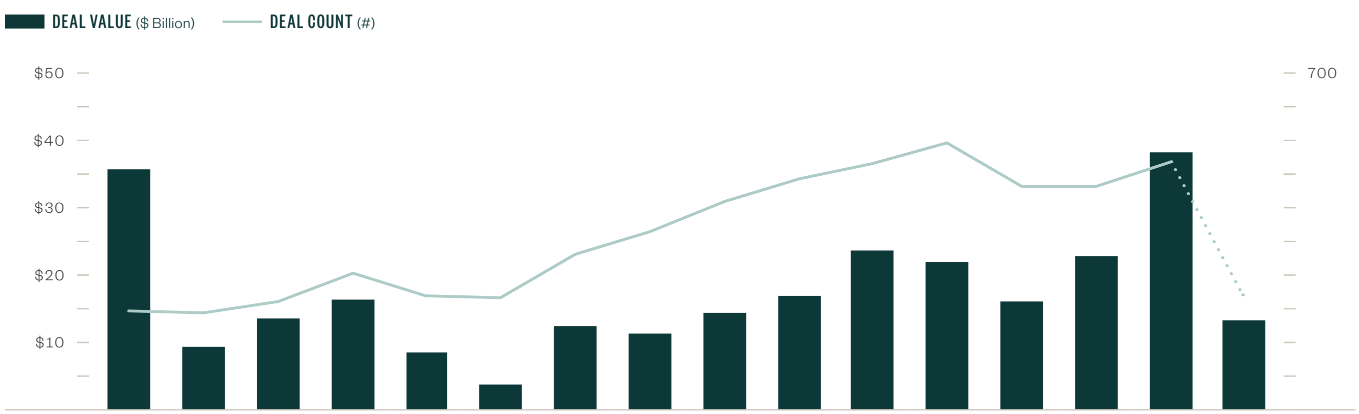
* As of August 6, 2019

The venture industry has matured and grown in sophistication; and more firms are willing to gain exposure across geographies at the early stage after their investment strategies have been proven in domestic ecosystems.

EARLY-STAGE EXITS

The steady stream of liquidity for investors in those early stages has been critical to the boom in early-stage deal making.

FIGURE 7: Early-Stage VC Exit Activity: Deal Value and Deal Count
United States, 2004–2019 YTD



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019*
Value	$31.5	$8.1	$11.9	$14.4	$7.4	$3.3	$11.0	$9.9	$12.6	$14.8	$20.7	$19.3	$14.1	$19.9	$33.6	$11.6
Count	226	220	247	309	259	254	356	408	477	526	562	607	511	511	567	259

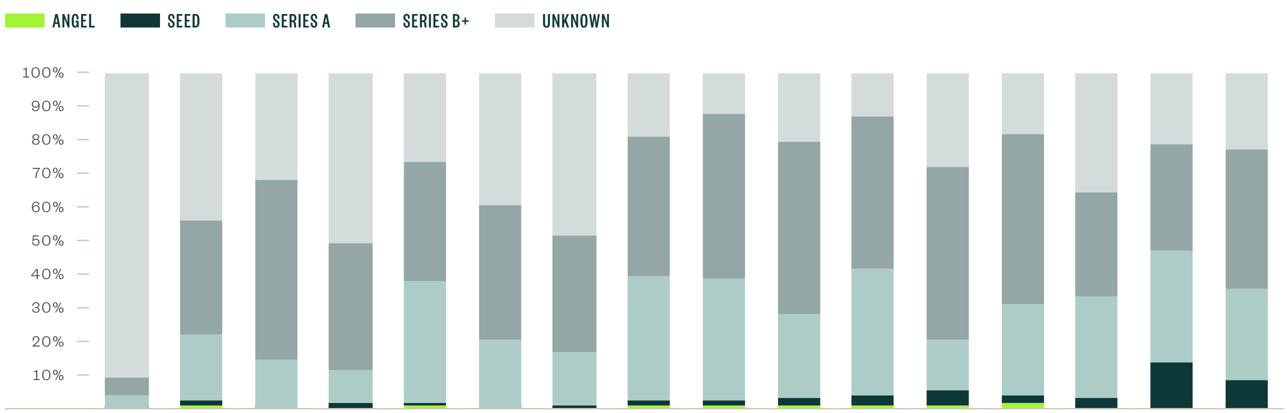
* As of August 6, 2019

So much heed has been paid to the unicorn phenomenon and the tendency of companies to stay private for longer that other trends can be ignored. However, many companies may raise a few rounds of funding and then continue growth without raising further funds, thus staying private while having only raised early-stage financings.

PitchBook's exits data on early-stage VC-backed companies suggests this may be the case. In 2018, companies that had raised only up to Series B+ stock exited to an aggregate value of $33.6 billion across 567 sales. The bulk of such exits understandably occurred where the last financing type was Series A or B, although a record surge in post-seed-only exit value was notched in 2018.

Outliers can skew some of those figures, of course, especially in pharma and biotech where a preclinical company can exit for a vast sum. However, the overall health of exit activity among companies at the early stage signifies the increasing sophistication and scale of the companies themselves.

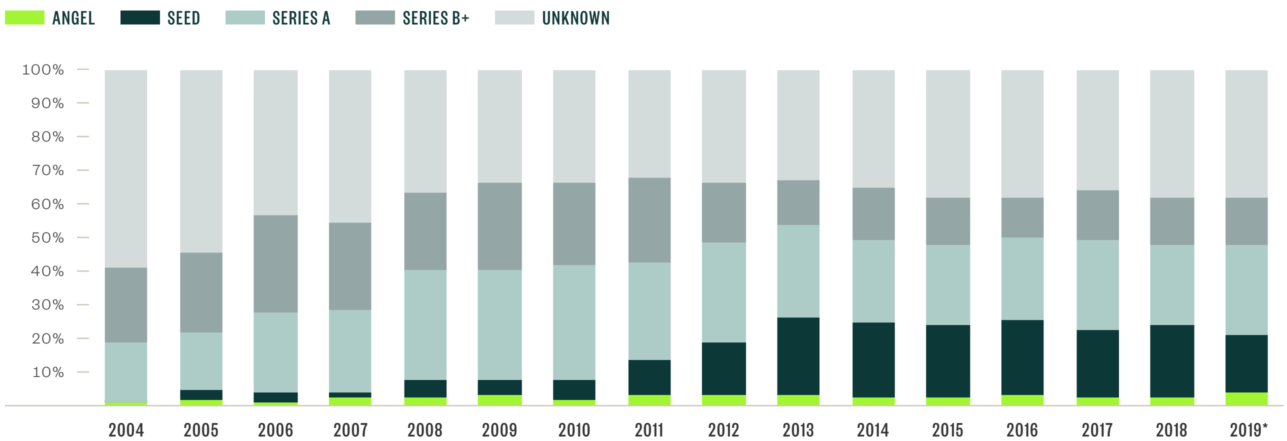
FIGURE 8: Early-Stage VC Exit Activity: Percentage Deal Value by Stock Type
United States, 2004–2019 YTD, ($ Billion)



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019*
Angel	$0.1	$0.1	$-	$0.1	$0.1	$0.0	$0.0	$0.1	$0.2	$0.1	$0.2	$0.2	$0.2	$0.1	$0.0	$0.0
Seed	$0.0	$0.1	$0.0	$0.2	$0.0	$0.0	$0.1	$0.2	$0.2	$0.3	$0.5	$0.8	$0.4	$0.6	$4.5	$0.9
Series A	$1.2	$1.6	$1.7	$1.4	$2.7	$0.7	$1.7	$3.7	$4.6	$3.7	$7.9	$3.0	$3.8	$6.0	$11.3	$3.2
Series B+	$1.6	$2.8	$6.4	$5.5	$2.7	$1.3	$3.8	$4.1	$6.2	$7.7	$9.5	$9.8	$7.1	$6.2	$10.6	$4.9
Unknown	$28.5	$3.6	$3.8	$7.3	$1.9	$1.3	$5.3	$1.8	$1.5	$3.0	$2.6	$5.4	$2.6	$7.1	$7.1	$2.6

* As of August 6, 2019

FIGURE 9: Early-Stage VC Exit Activity: Percentage Deal Count by Stock Type
United States, 2004–2019 YTD



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019*
Angel	1	3	1	6	6	8	5	11	15	13	13	13	13	10	11	9
Seed	1	7	8	5	13	10	22	44	74	123	124	129	117	102	123	45
Series A	39	37	58	75	84	83	120	117	143	145	138	145	124	138	137	69
Series B+	51	52	73	82	60	67	89	104	84	73	89	87	60	75	81	37
Unknown	134	121	107	141	96	86	120	132	161	172	198	233	197	186	215	99

* As of August 6, 2019

With median pre-money valuations and financings soaring in size, companies can grow faster and to a greater scale if they retain discipline and efficiency in spending. Total accessible markets are also growing given proliferation of digitization and mobile overall. Consequently, when they do sell, they are able to command a heftier price.

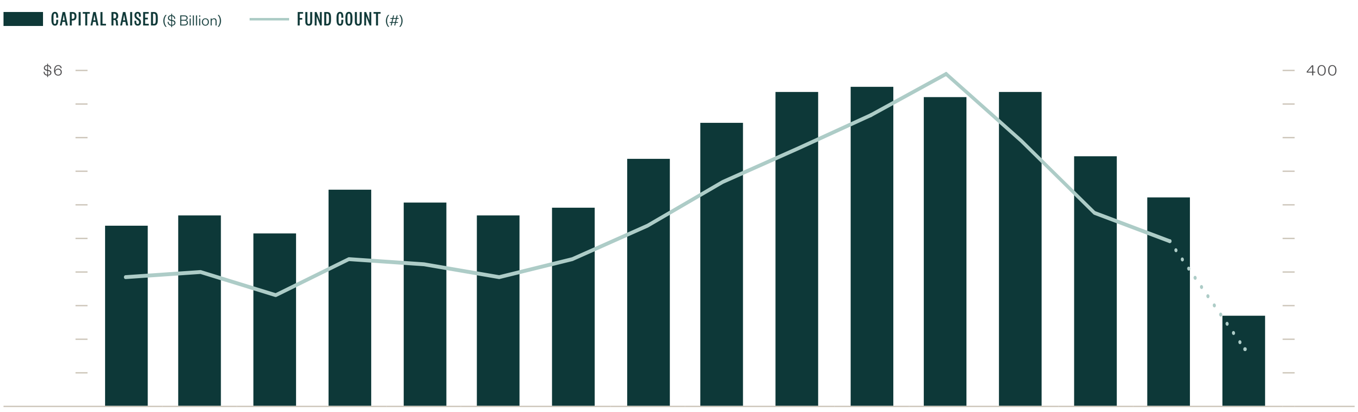
Increasing sophistication of available tools and total market potential are also contributing to healthy exit trends. Relative to five to 10 years ago, companies can reach a vast market and utilize more advanced tools across a broad swath of business operations, thereby scaling faster (such as WhatsApp, which raised a Series B and then was acquired for $22 billion). While WhatsApp is clearly an outlier, its business model and operations would not have been feasible 10 years ago.

EARLY-STAGE FUNDRAISING

The final key driver of the robust early-stage investment cycle is the healthy early-stage fundraising market that has persisted for most of this decade.

It's difficult to parse out the funds that deal exclusively in one area of early stage as fund mandates often require more flexibility. However, analyzing fundraising activity of $50 million or less tends to be the most useful comparable, given angel and seed financing and valuation trends. In addition, comparing such fundraising activity to market size ranges between $50 million and $100 million helps paint a clearer picture of the market reality.

FIGURE 10: Early-Stage VC Fundraising Activity: Deal Value and Deal Count
United States, 2004–2019 YTD, Fund Size <= $50 Million

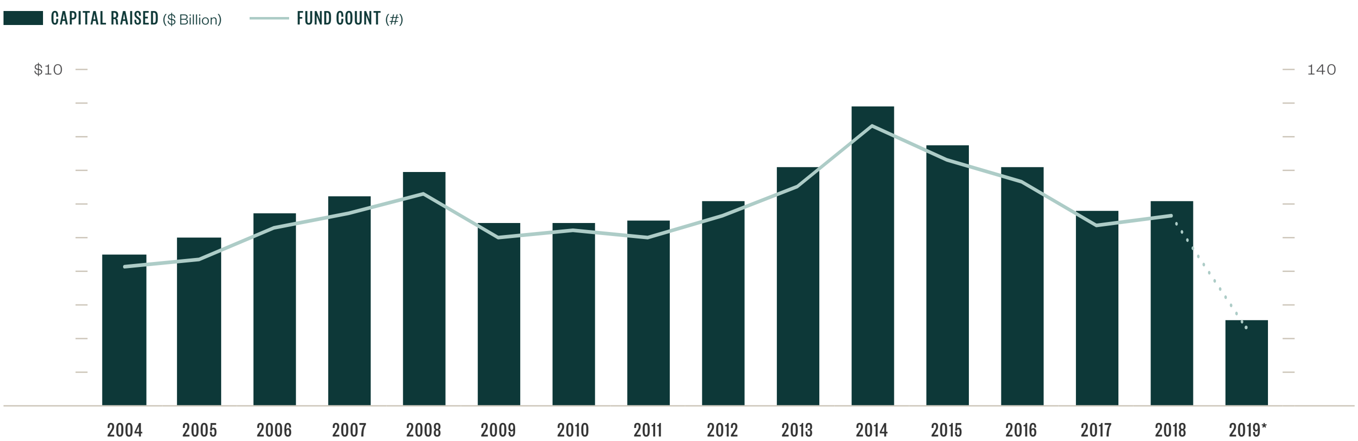


	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019*
Value	$3.0	$3.2	$2.9	$3.6	$3.4	$3.2	$3.3	$4.2	$4.8	$5.3	$5.4	$5.2	$5.3	$4.2	$3.5	$1.5
Count	143	150	123	166	158	145	164	202	252	288	326	372	299	216	184	64

* As of August 6, 2019

The surge in $50 million or less fundraising volume that crested in 2015 has significantly helped fuel overall early-stage deal making. Its diminution, however, is explained in part by the steadiness of fundraising figures one size bracket higher, between $50 million and $100 million.

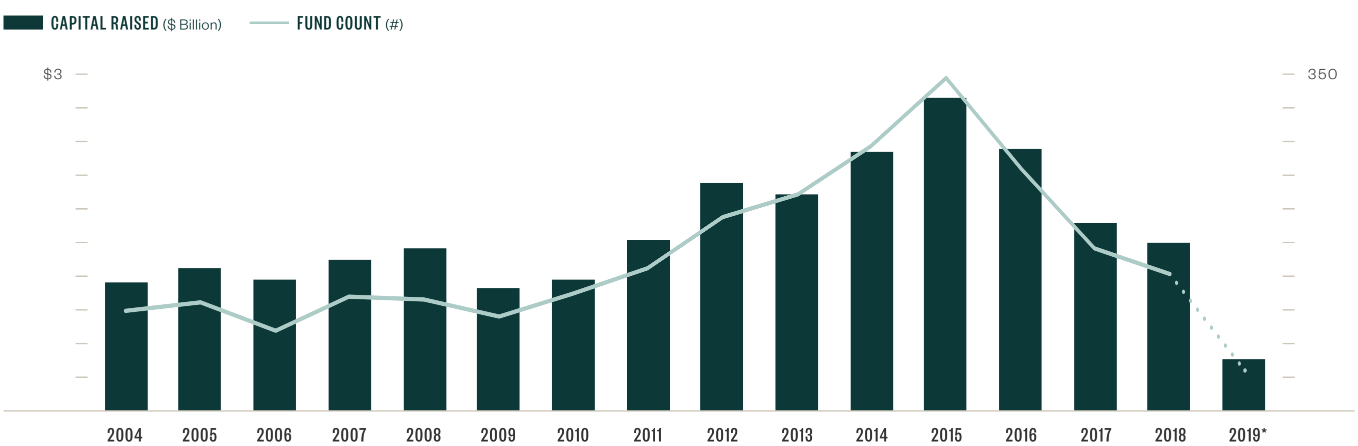
FIGURE 11: Early-Stage VC Fundraising Activity: Deal Value and Deal Count
United States, 2004–2019 YTD, $50 Million <= Fund Size <= $100 Million



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019*
Value	$4.4	$5.0	$5.7	$6.2	$7.0	$5.4	$5.4	$5.5	$6.1	$7.1	$8.9	$7.7	$7.1	$5.8	$6.1	$2.5
Count	58	61	74	80	88	70	73	70	79	91	116	102	93	75	79	32

* As of August 6, 2019

FIGURE 12: Early-Stage VC Fundraising Activity: Deal Value and Deal Count
United States, 2004–2019 YTD, Fund Size <= $25 Million



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019*
Value	$1.0	$1.1	$1.0	$1.2	$1.3	$0.9	$1.0	$1.3	$1.7	$1.7	$2.0	$2.4	$2.0	$1.4	$1.3	$0.4
Count	90	97	73	102	100	86	104	129	174	193	236	298	217	146	122	36

* As of August 6, 2019

Fund managers that were successful in seed, pre-seed, and Series A investing in the first half of the 2010s raised larger follow-on vehicles to continue investing in the second half, both to scale and adapt to increasingly inflated market conditions. While some investors chose to invest within their familiar unit economics, trends are similar across the broader spectrum since 2014.

After a crest in activity for all size segments in the first half of the 2010s, volume subsided even while capital raised remained robust. That divergence is due to:

- A mix of the discontinuation of unsuccessful funds
- The timing of when funds that raised at the peak choose to embark on the fundraising trail again
- An adaptation to costlier and more competitive market conditions.

Looking forward, it's likely that an equilibrium of sorts will be achieved between those drivers, especially as the newest crop of funds work through the extant early-stage ecosystem and find either success or failure.

> "If we do experience a general market correction (a recession, for example) in the near term, there should be a period where VC is still deploying capital to keep existing investments afloat and to avoid returning capital to their investors. But they may not fund as many new investments."

– CHERYL TEETER-BALIN

METHODOLOGY

- Early-stage VC activity is defined as venture financing wherein the PitchBook deal type is angel, seed, and early-stage VC (Series A and B, typically).
- VC-backed exits as of the early stage are defined as exits that occurred for companies that had their last round of financing classified as early stage.
- All data is as of August 6, 2019, and compiled by PitchBook.

About Moss Adams

With more than 3,200 professionals across 25-plus locations in the West and beyond, Moss Adams provides the world's most innovative companies with specialized accounting, consulting, and wealth management services to help them embrace emerging opportunity. Discover how Moss Adams is bringing more West to business.

mossadams.com/technology

mossadams.com/lifesciences

mossadams.com/communications