



Silicon Valley Bank

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Innovation Economy Outlook 2016

U.S. STARTUP OUTLOOK 2016

New reality prompts U.S. startups to focus on fundamentals



Letter from SVB's CEO

We are pleased to present Startup Outlook 2016, Silicon Valley Bank's annual report on the health of the innovation economy. For each of the past seven years, we have taken a survey of companies to learn what entrepreneurs are thinking about business conditions, access to capital and talent, and the policy issues that help or hinder their success.

This year, we are drawing on responses from more than 900 technology and life science executives, and for the first time we expanded the survey to China. SVB conducted the survey portion of the report in December 2015, just as significant market volatility was taking hold. They say timing is everything, and in the past several weeks it has become apparent that entrepreneurs' perceptions at the end of 2015 had already shifted by mid-January.

The public conversation about 2016 is filled with doom and gloom about the innovation sector, with exaggerated predictions of the death of unicorns, a funding crisis and lackluster results all around.

At Silicon Valley Bank, we see it differently. We think it's a healthy recalibration but it doesn't mean it's going to be easy for entrepreneurs.

Valuations were high, now they are coming back to earth. Growth at any cost is being replaced with a focus on profitability. Companies were priced for perfection, and we may see some stumble or even go out of business.

Entrepreneurs we speak with, while remaining naturally optimistic, are adopting a new attitude: Be prepared. They are pulling the reins tighter on operations and retooling strategies. They are anticipating a more balanced funding environment. They are considering M&A an even more viable exit strategy. In 2016, access to capital will get harder. But it's not supposed to be easy, and there will be opportunities for good companies with good ideas. That's healthy.

Thank you for taking a look at this report. We hope the findings can be useful as you chart your own path or follow this sector. Looking globally, the opportunities for innovation are abundant. Entrepreneurs are strong-willed men and women who want to have a positive impact on the world. That's never going to change.



Greg Becker

President and CEO, Silicon Valley Bank

In 2016, the byword is prepare. The economic outlook is shifting, according to U.S. technology and life science startup executives surveyed in late 2015 for Silicon Valley Bank's annual outlook. Capital is tightening and inflated valuations are declining, prompting companies to adjust to a more balanced funding environment and focus on fundamentals. Executives said they expected M&A to maintain its importance as an exit strategy, venture capital to be a vital funding source and attracting top talent to be a critical challenge. And, while the bottom line may be taking a hit short term, optimism about the long-term future of innovation is not.

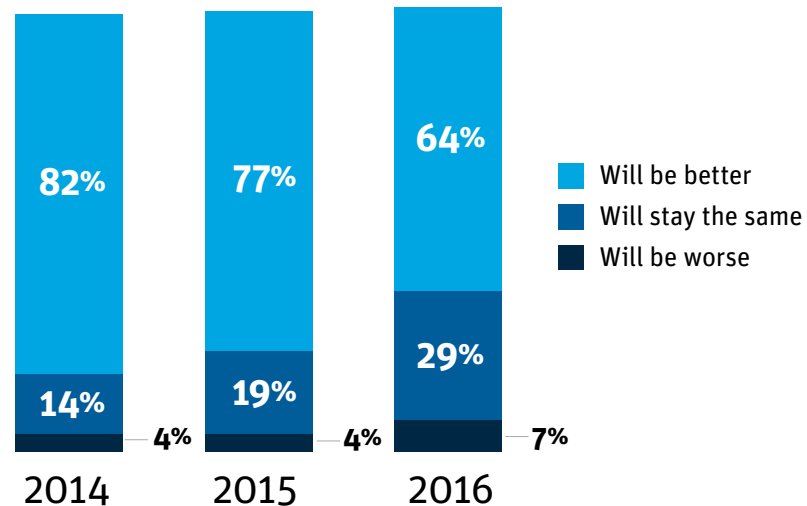
Startups temper their positive outlook

Sixty-four percent say business conditions will be better than 2015. That said, it represents an 18 percentage point drop over the last two years. Unbridled optimism has been replaced with rational restraint.

Describe your outlook on business conditions for your company this year compared to last.

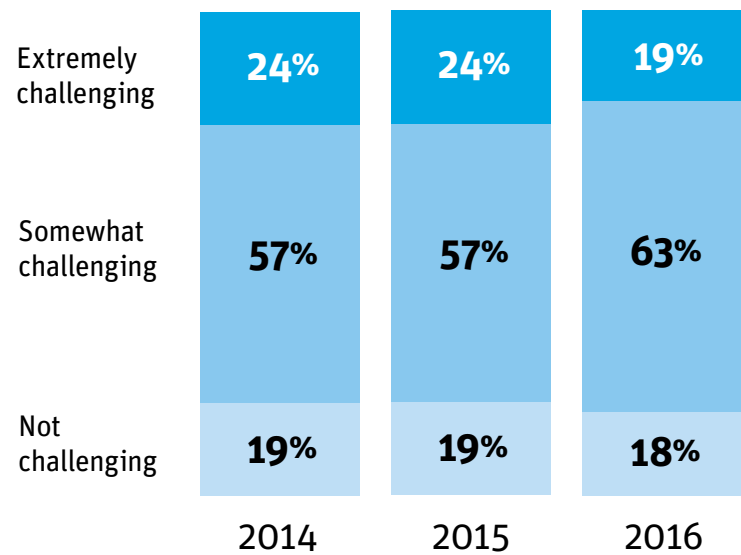
“The innovation economy will always thrive in the long run. There will be bumps along the way.”

– Northern California consumer Internet executive



Raising money continues to be challenging

Most executives said the fundraising environment was extremely or somewhat challenging, and 21 percent named access to financing as their single biggest challenge in running their businesses. Raising money is always challenging, and tightening capital requirements often lead to healthier, more sustainable companies.



What is your view of the current fundraising environment?

A full 82% of leaders surveyed said that fundraising is challenging, which is consistent with responses over the last three years.

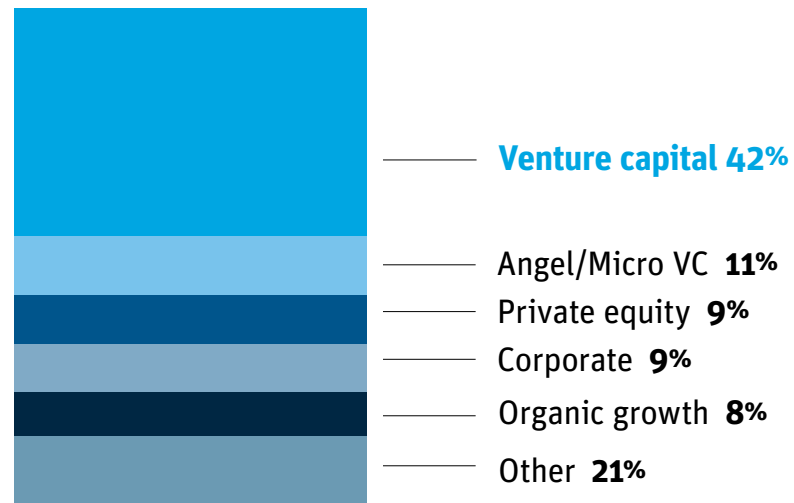
Startups say venture capital is critical to grow

At the end of 2015, survey respondents said they planned to seek venture capital more than other funding sources. Forty-two percent of executives expected venture capital to be their next source of funding, with angel investment a distant second. We expect that venture fundraising will become more challenging in 2016, but that VC investment activity will remain healthy.

What do you expect your company's next source of funding will be?

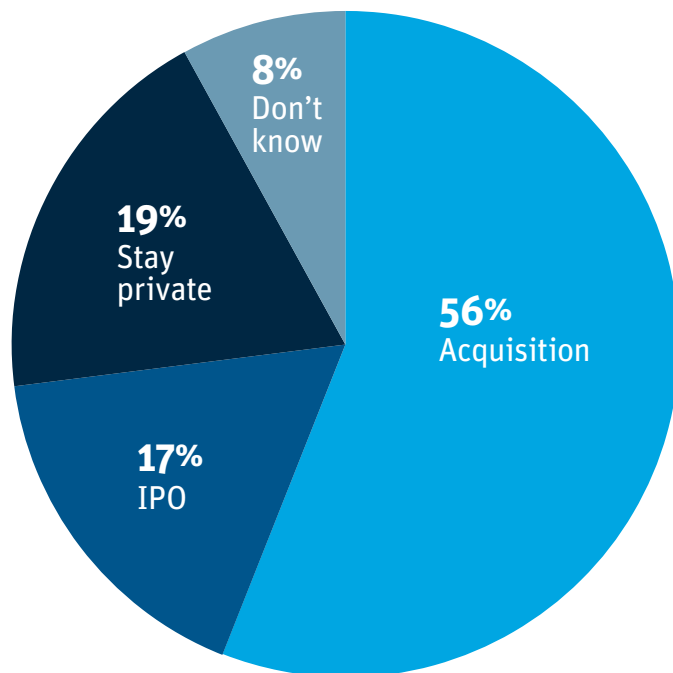
“My sense is that VC fundraising may be more difficult. But I think that good companies will still be able to find funding.”

– Georgia consumer Internet and digital media executive executive



Half of startups say their goal is an M&A exit

Acquisition continues to eclipse IPOs as the realistic long-term exit strategy of U.S. entrepreneurs. More than half of innovators set their sights on an acquisition, and nearly 20 percent aspired to stay private.

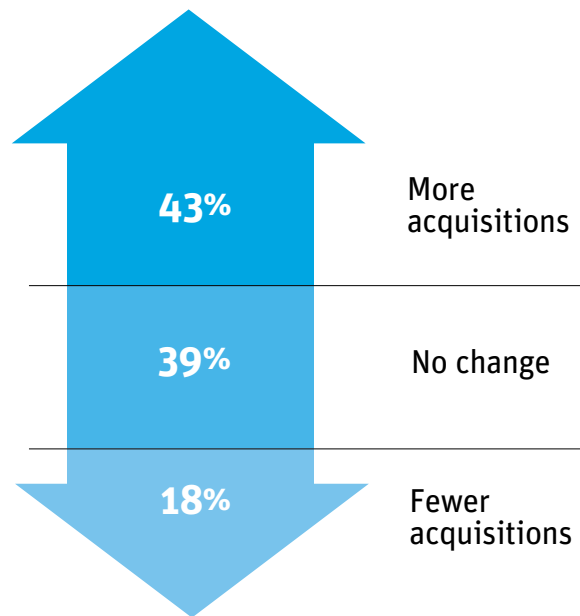


What is the realistic long-term goal for your company?

Among the startup executives surveyed, 56% said their long-term goal is to be acquired. Just 17% said they are aiming for an IPO.

M&A expected to be robust for 2016

Most startups said they expected acquisitions would increase or stay the same in 2016. Many tech IPOs faltered in 2015, making M&A a more viable exit option. Also, reduced valuations make acquisitions more attractive for top acquirers that have plenty of cash on hand to make significant purchases.



How do you think the M&A market will change over the next 12 months?

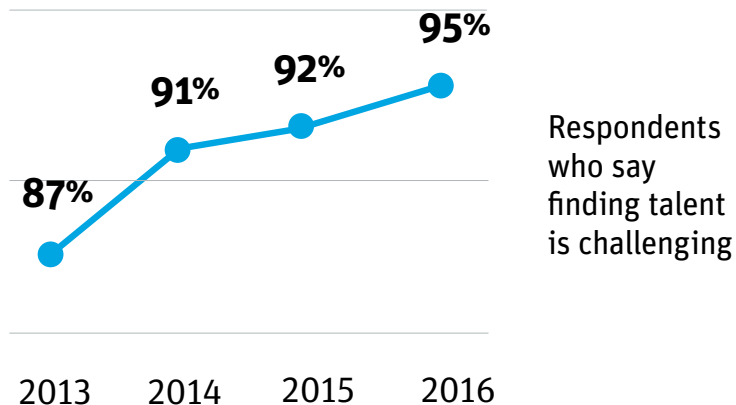
Of the leaders surveyed, 82% said they expect as many or more acquisitions than 2015.

It's hard to find the right talent

A full 95 percent of executives said it was challenging to find people with the skills necessary to help grow their businesses—an increase of 8 percentage points since 2013. After years of increasing difficulty finding the right talent, it's possible that the talent crunch has reached its peak and the very tight labor market may loosen. Even so, finding employees with the right skills will remain difficult in an overall environment of low unemployment rates.

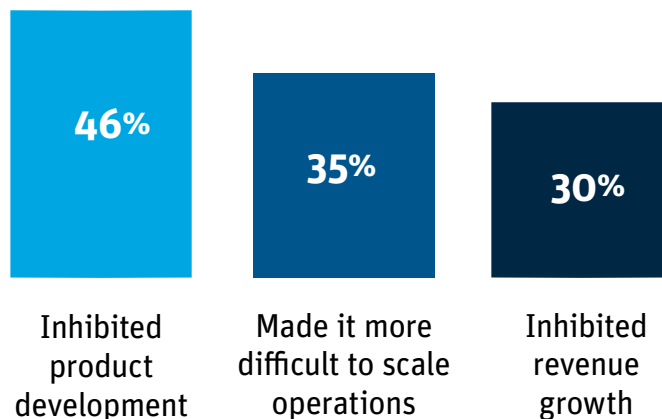
How challenging is it to find workers with the skills necessary to grow your business?

95% of entrepreneurs said it's challenging, compared with 87% just three years ago.



Lack of skilled workers hurts the bottom line

Of the leaders surveyed, 17 percent said recruiting was their biggest challenge. Half of the respondents said they were looking for engineering and technical skills. Sales, product development and marketing skills are also critical needs this year. The lack of skilled workers creates measurable business impacts, such as inhibiting product development, making it harder to scale operations and inhibiting revenue growth.



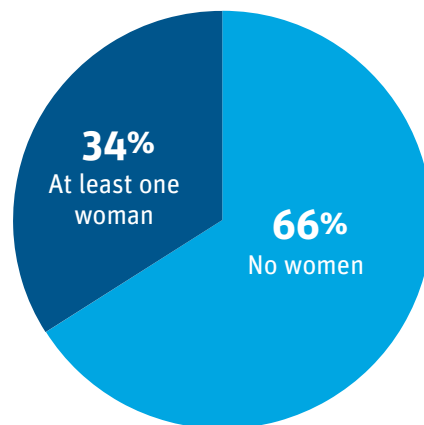
How has the lack of access to talent affected your company?

Innovation executives said the lack of skilled workers inhibited product development and made it difficult to scale operations.

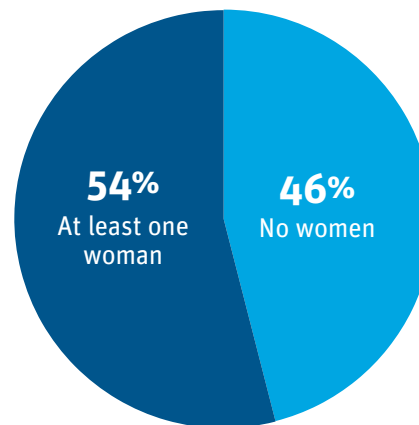
Note: Respondents were given the opportunity to select multiple responses.

Startups have few women in leadership positions

It's well documented that women are underrepresented in startup leadership positions: 66 percent of startups have no women on their boards, and nearly half (46 percent) have no women in executive positions. About a quarter of respondents (26 percent) said they have programs in place to increase the number of women in leadership roles. Creating more diversity in the top ranks of all companies is an imperative, and the dialogue on how to make it happen needs to continue.



Women on the board



Women in executive positions

How many women are in leadership positions within your company?

Among the startups surveyed, 66% don't have any women on their boards, and 46% have no women in executive positions.

Access to talent is the No. 1 policy issue for startups

Half of the survey respondents said access to talent was the most important public policy issue on their minds. Cybersecurity was also a key concern. Entrepreneurs typically don't embrace government action but do believe the federal level should play a role by funding research to combat cyberattacks, creating uniform rules for data breaches and sharing best practices for preventing and responding to them.

What are the most important public policy issues affecting companies like yours?

Half of the startups surveyed said access to talent is the most important policy issue, followed by cybersecurity and healthcare costs.

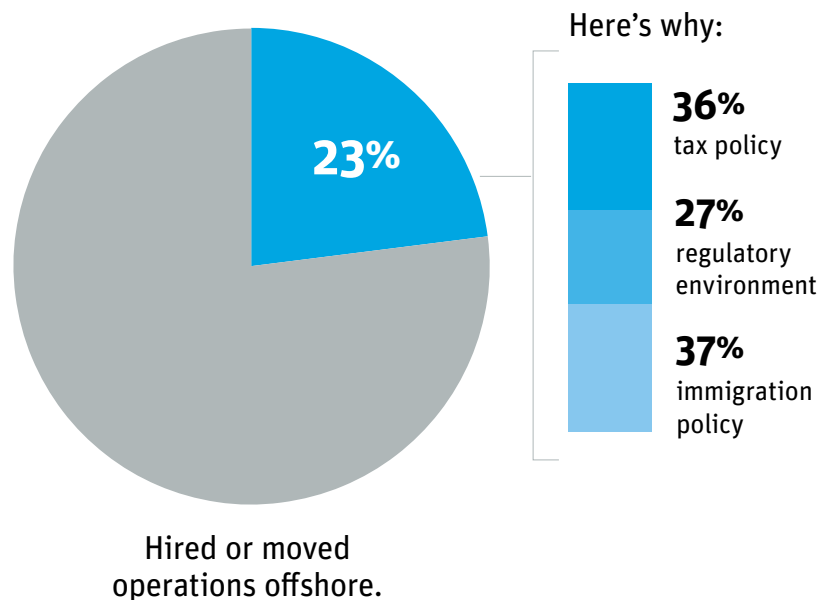


1. Access to talent 50%
2. Cybersecurity 36%
3. Healthcare costs 33%
4. Consumer privacy regulation 23%
5. Patent litigation 23%

Note: Respondents were given the opportunity to select multiple responses.

Some startups say regulations are driving operations offshore

One in four respondents said regulations were prompting them to locate facilities or move non-sales operations outside the U.S. Startups on a shoestring budget are sometimes motivated to set up shop where it costs less to do business and it's easier to find skilled workers.



Have U.S. laws and regulations materially affected your company's decision to locate facilities or hire employees for operational non-sales activities outside the U.S.?

Half of the startups surveyed said regulations are growing and 23% said they had hired or moved operations offshore.

About the Startup Outlook 2016 survey

Our seventh annual survey of technology and healthcare executives offers insight into what's on the minds of innovation leaders today. For this year's survey, we received more than 900 responses, covering such topics as how innovation companies are faring, hiring projections and how government policies are affecting business growth.

Total
respondents

929

Industry sector



68%
Technology
(net)



15%
Healthcare
(net)

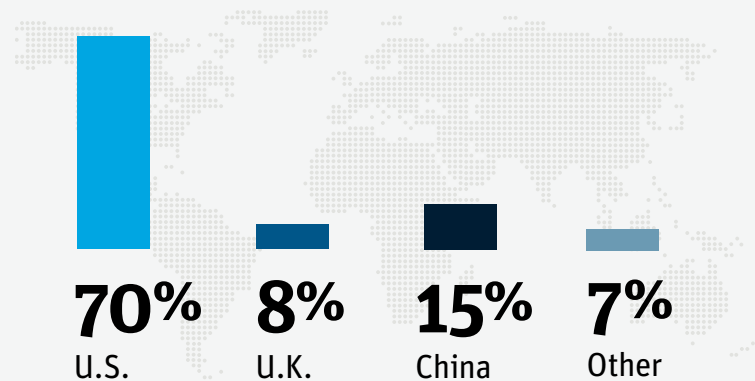
17%
Other

Profitable

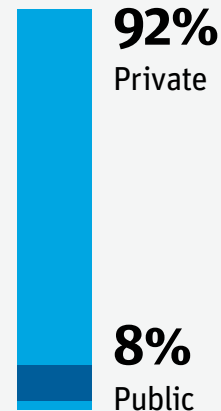


45% Yes
55% No

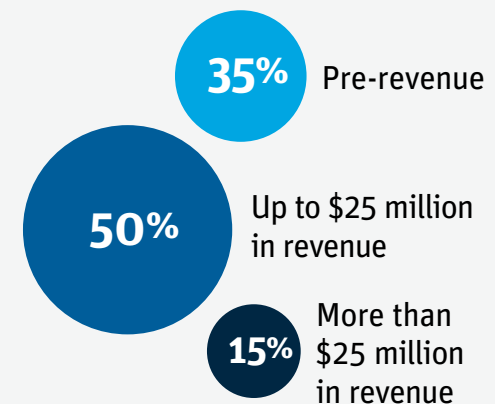
Primary place of business



Ownership



Revenue stage





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About Silicon Valley Bank

For more than 30 years, Silicon Valley Bank (SVB) has helped innovative companies and their investors move bold ideas forward, fast. Silicon Valley Bank is the California bank subsidiary of SVB Financial Group (Nasdaq: SIVB). With commercial, international and private banking services, SVB helps address the unique needs of innovators. Forbes named SVB one of America's best banks (2015) and one of America's best-managed companies (2014).

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A third-party firm, Peerless Insights Survey, conducted the Innovation Economy Outlook 2016 survey online on Silicon Valley Bank's behalf from November 12, 2015, to January 6, 2016.

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