

svb



Silicon Valley Bank

Q3
2020

State of the Markets

Silicon Valley Bank's Inside View of
the Global Innovation Economy



State of the Markets: Third Quarter 2020



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A Scattered Recovery is Taking Shape

To say the world has been shaken in the past four months is an understatement. The Great Lockdown caused a global output shortfall of \$12.5 trillion. Governments have reached deep into their coffers to inject relief into shocked economies. We've seen companies bolster balance sheets via debt issuance and trim expenses, including layoffs.

Like many early recoveries, this is a time of contradictions. Growth rounds continue as the late-stage has restored momentum; early-stage companies and small GPs have faltered. Certain sectors are hotter now than ever before; countless others have faced headwinds. The tech IPO window has cautiously reopened, whereas the healthcare window never closed.

As we know, and has become increasingly apparent in recent months, innovation touches every aspect of our lives, revealing an even greater need for inclusivity and diversity in the innovation economy. In this report's Social Impact section, the data describes the lack of diversity among tech companies and venture capital investors and trends around investing for social impact. The gaps are glaring, and we all need to take a more active role to close them.

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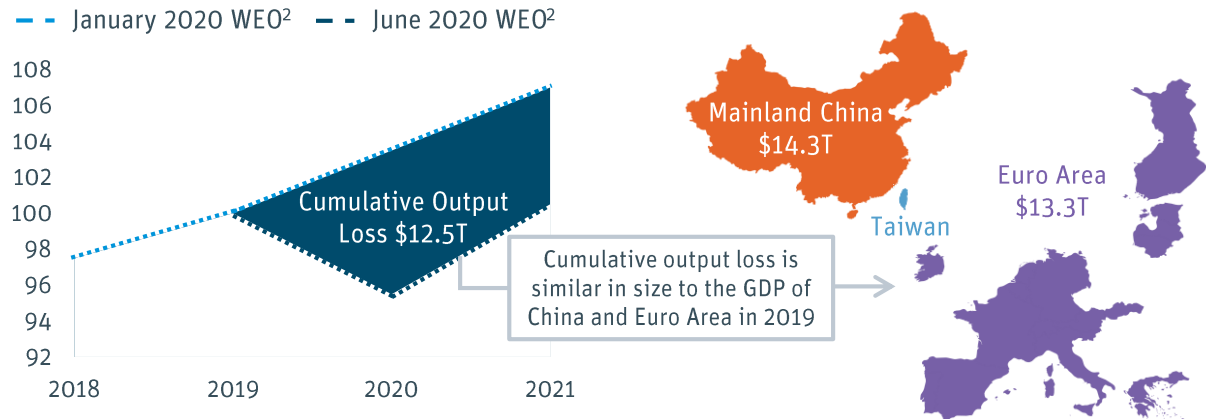
Global Economy on Unstable Footings



Comeback Season?

After the worst Q1 in history, equity markets have roared back to nearly pre-COVID-19 levels. The S&P 500's performance in Q2 marked the best quarterly return since 1998, when markets soared following the summer crash driven by events in Russia and Asia. While markets have recovered, the economic outlook remains bleak. The International Monetary Fund (IMF) estimates a cumulative loss to the global economy of \$12.5T over the next two years due to the Great Lockdown — rivaling the size of China's and Euro Area's GDP¹. This lost output brings into question the robustness of the markets' recovery.

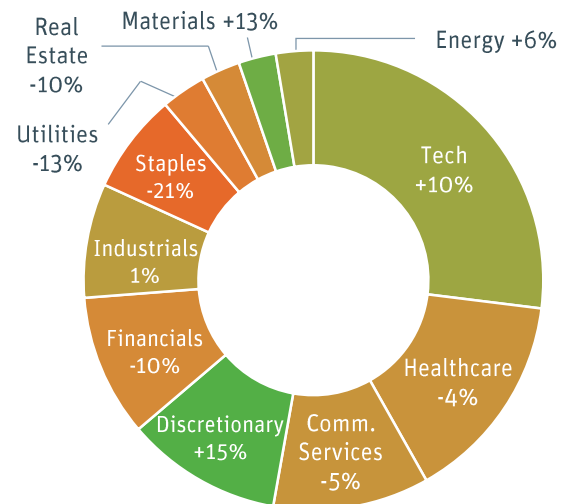
Output Loss Due to COVID-19 Scaled by Select Country GDP¹



Top S&P 500 Quarterly Returns Since 1998

Quarter	S&P 500 (↓)	Tech ³	Comm ³
Q4 1998	21%	36%	28%
Q2 2020	20%	30%	20%
Q2 1997	17%	23%	12%
Q2 2009	15%	19%	2%
Q3 2009	15%	17%	4%
Q2 2003	15%	18%	20%
Q4 1999	15%	36%	9%
Q1 1991	14%	14%	3%
Q1 1998	14%	21%	17%
Q1 2020	-20%	-12%	-17%

S&P 500 Sector Relative Performance Since Trough⁴

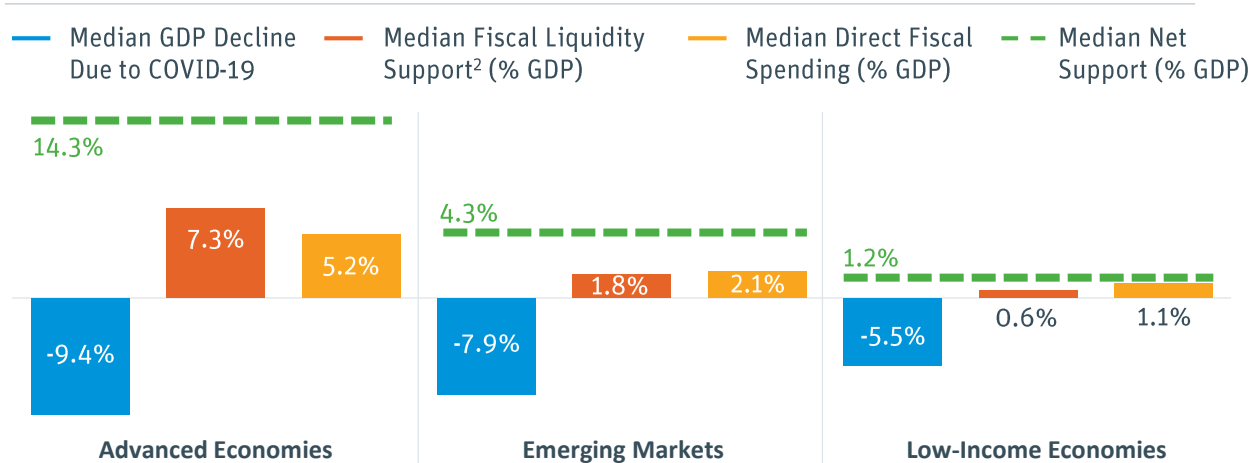


Relief Flows into (Parts of) the Economy

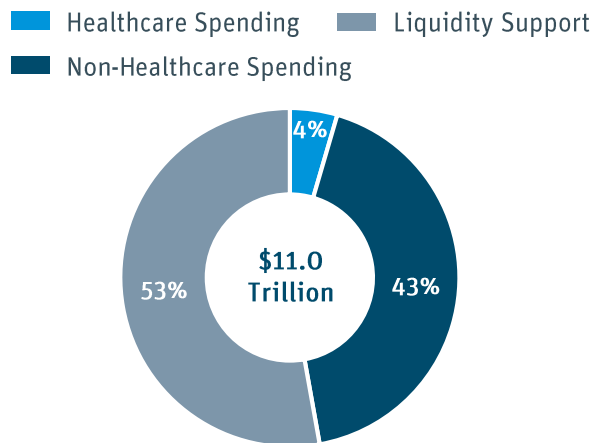
In the face of a \$12.5T hit to global GDP output, governments around the world have responded by introducing historic stimulus measures. Approximately \$11.0T has flowed into the global economy, though the lion's share has gone to advanced economies. Stimulus received by emerging and low-income economies has, by contrast, been severely disproportionate to their economic damage.

This deficit could jeopardize the gains of certain innovation economies, most notably in India, Latin America, and Africa.

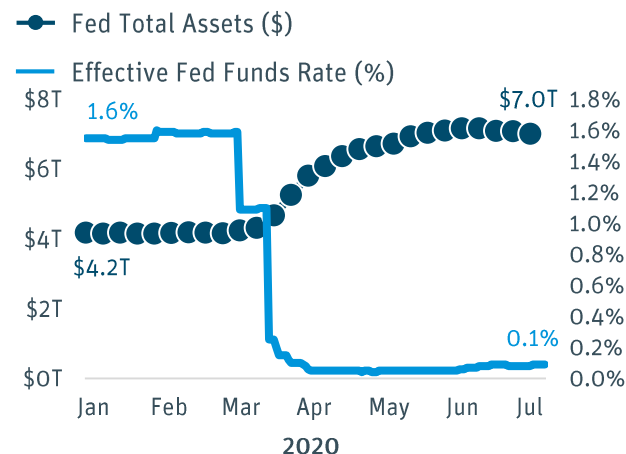
GDP Growth and Stimulus Spending as a Percentage of GDP¹



Stimulus Spending by Use



Federal Reserve Balance Sheet

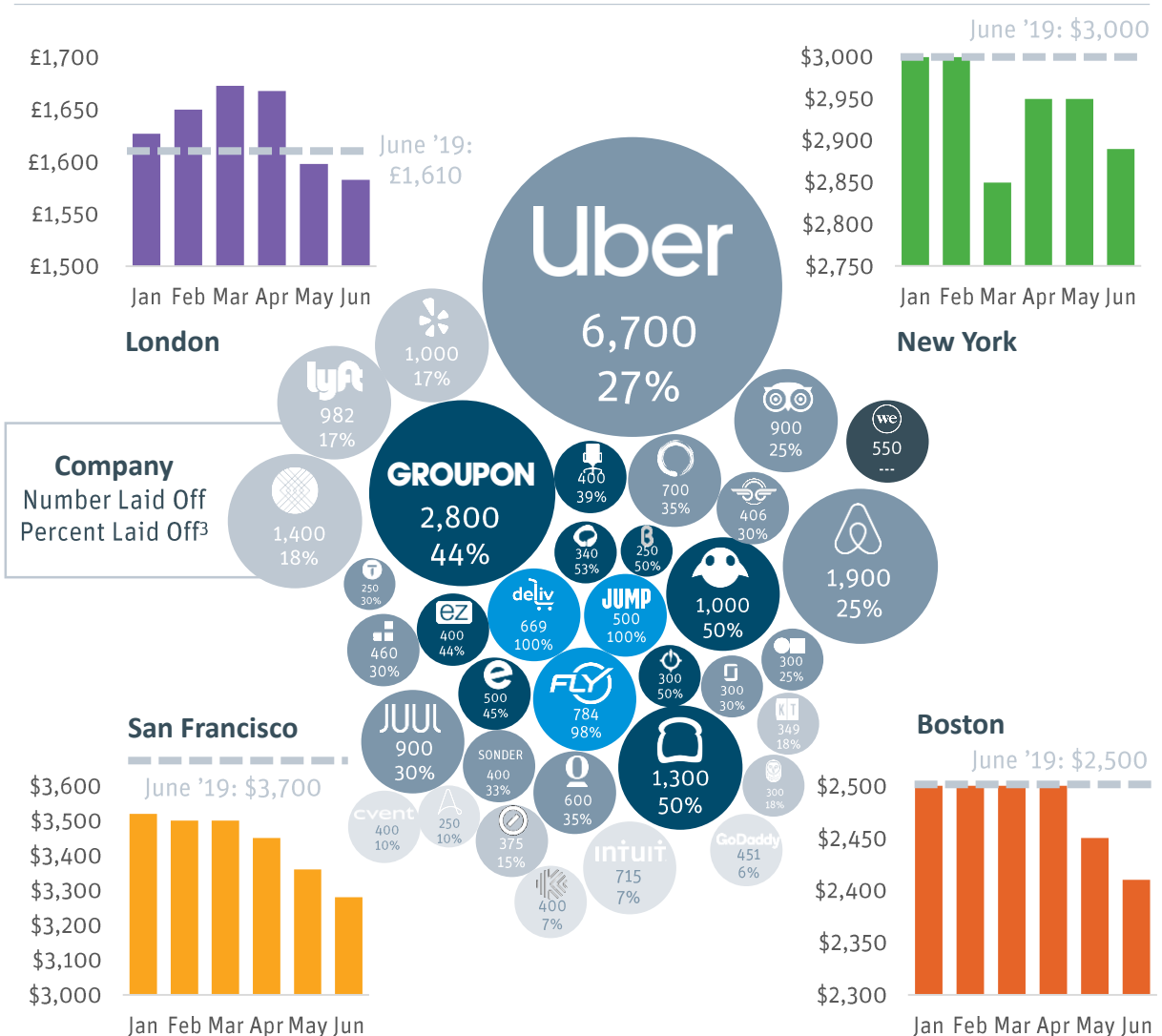


Layoffs Ripple Across Startups

Layoffs have swept the startup ecosystem — with some startups laying off thousands of workers or nearly all their headcount. As a result of layoffs and mandated remote work, employees in the U.S. have left expensive metros, causing rent prices to fall — especially in tech-centric San Francisco. Similar trends have also transpired overseas with London, the U.K.’s major tech hub, experiencing falling rents.

Increasing adoption of distributed workforces could see emerging metros benefit from an influx of tech talent, which would have cascading effects on company formation, venture investment and the recycling of talent and capital.

Company Layoffs¹ and Major Tech Hub Rental Prices²

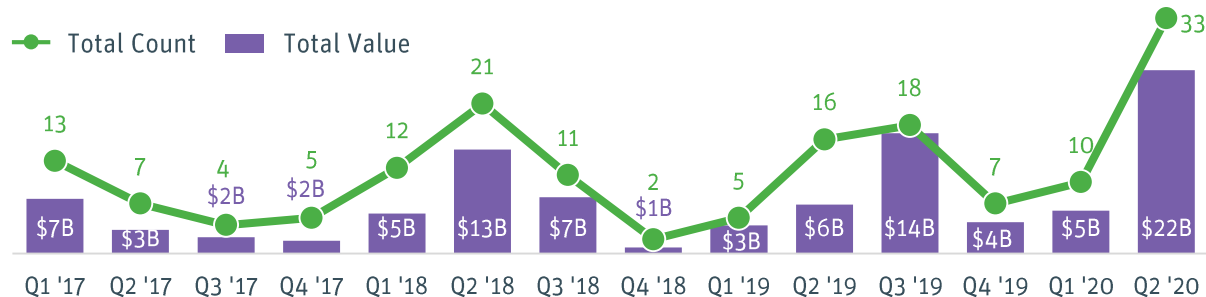
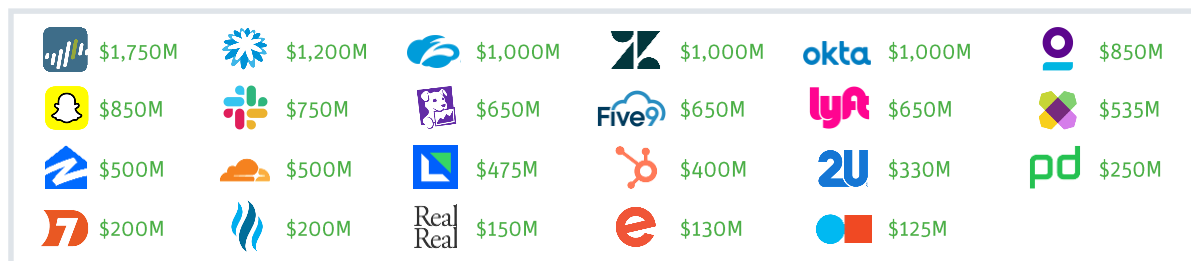


Note: 1) Based on company press releases and news articles. 2) Median rental price for a one bedroom except for London which is average rent for all properties based on the HomeLet Rental Index. 3) Percent laid off not available for WeWork. Source: Zumper, HomeLet, company press releases and SVB analysis.

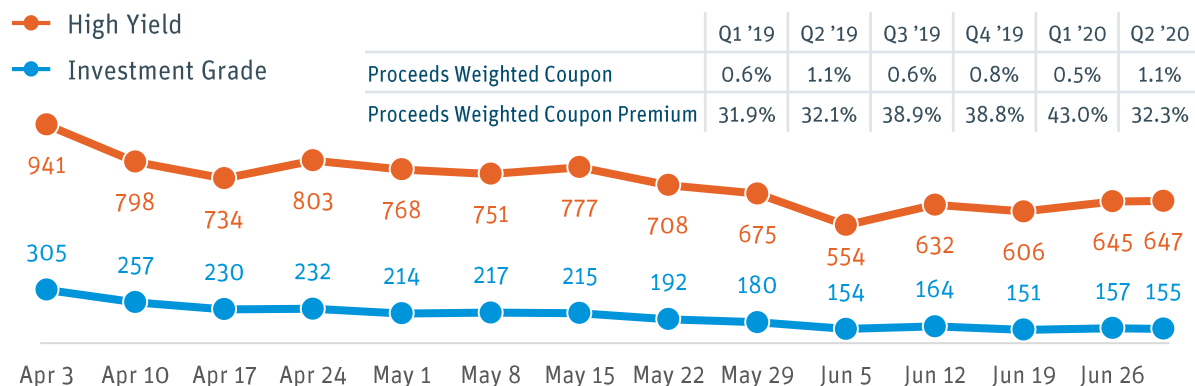
Convertible Debt Spikes

The convertible debt market saw its best quarter ever with more than \$57B of issuance in Q2. This pushed total first half issuance to \$68B — outpacing 2019’s full year total. Tech led the way with \$22B of issuances as notable tech giants — some of which were recent unicorns — tapped the debt markets to add liquidity in size. After shutting down in March, companies raced to issue converts, and this trend only accelerated as credit spreads and equity markets recovered. Additionally, supply dynamics played a role, with low-leverage corporates tapping bond markets to shore up balance sheets.

U.S. Tech Convertible Debt Issuance by Quarter



High Yield and Investment Grade Spread to Worst¹ During Q2



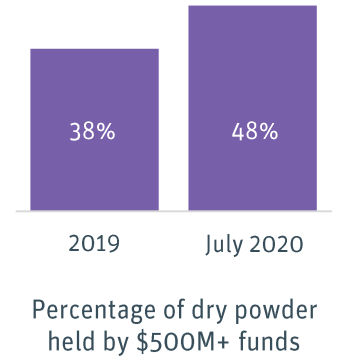
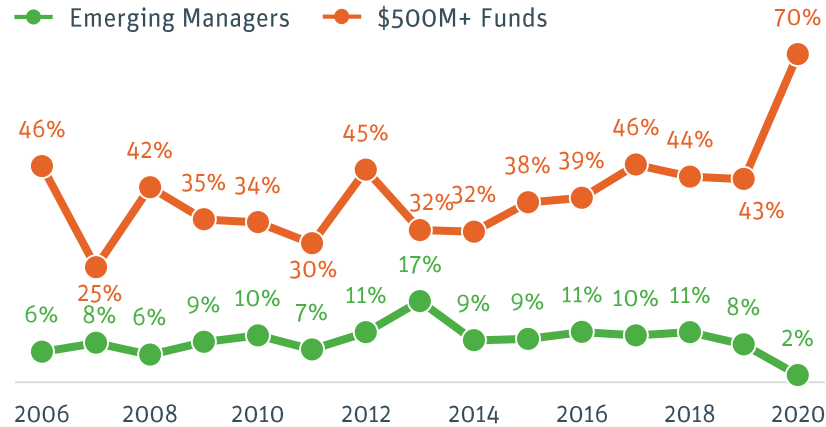
Private Markets

Varied
Impacts

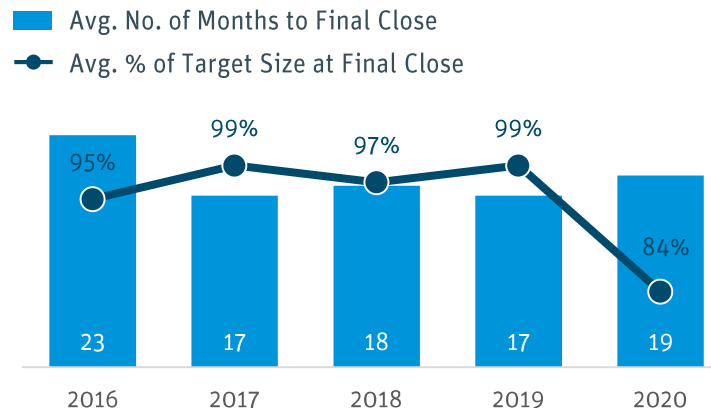
Top-Tier Funds Expand Their Share

Record levels of capital have entered venture, with H1 2020 boasting a 36% increase in the rate of fundraising over 2019. The majority of this capital has flowed to established VC firms. Less was allocated to emerging managers — who have seen a six percentage point decrease in their share of capital — in large part the result of strong fundraising for large funds. Furthermore, as LPs pause, funds have taken longer to close and reach a lower proportion of their target raise, suggesting an impending slowdown in VC fundraising for H2 2020.

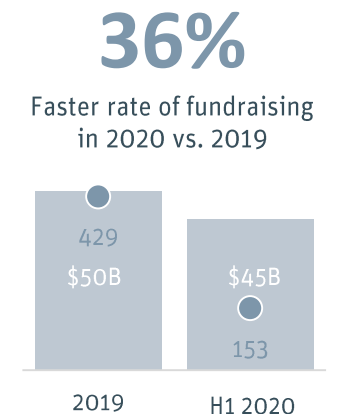
Emerging Managers¹ vs. \$500M+ Funds Share of Fundraising



VC Funds: Months to Close and Percentage of Target Size Secured²



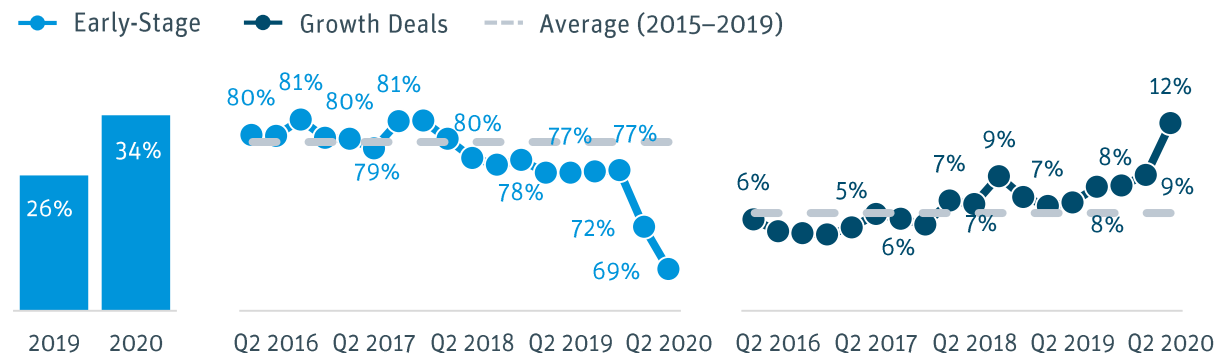
VC Fundraising²



Growth Rounds Grow, Early-Stage Falters

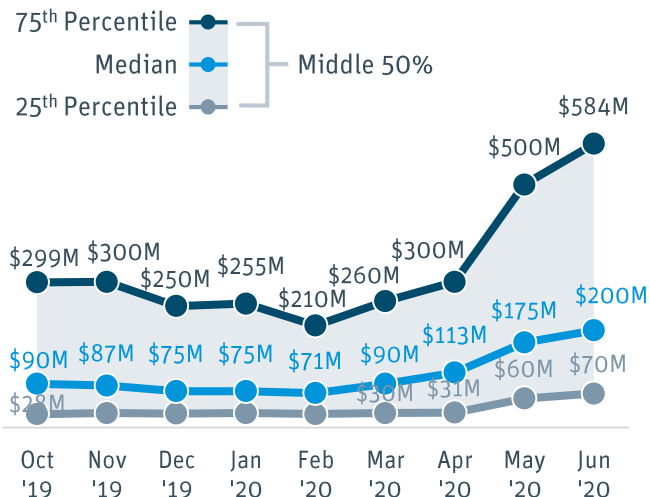
Angel deals persisted in Q2, while overall early-stage deals declined driven by challenges with remote networking and due diligence. In contrast, growth deals have continued, as they depend more on hard data and financials. Perceived “top” companies are in a league of their own, raising larger rounds at higher valuations, as investors double down on industry leaders, pushing valuations to record levels. Yet these top companies raised for various reasons. DoorDash and Instacart have raised growth equity whereas others have raised while resizing their cost structures and laying off employees.

U.S. Early-Stage and Growth¹ Deals as a Percentage of Deals

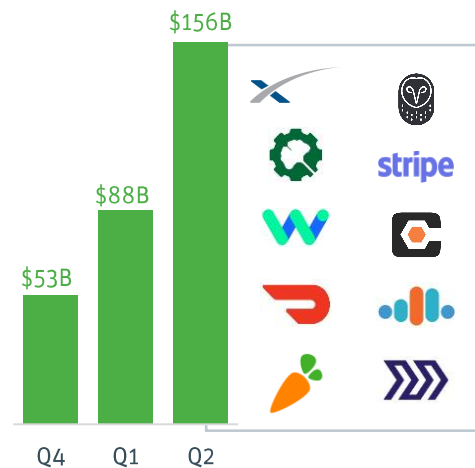


Angel deals share of early-stage

Late-Stage Pre-Money Valuations²



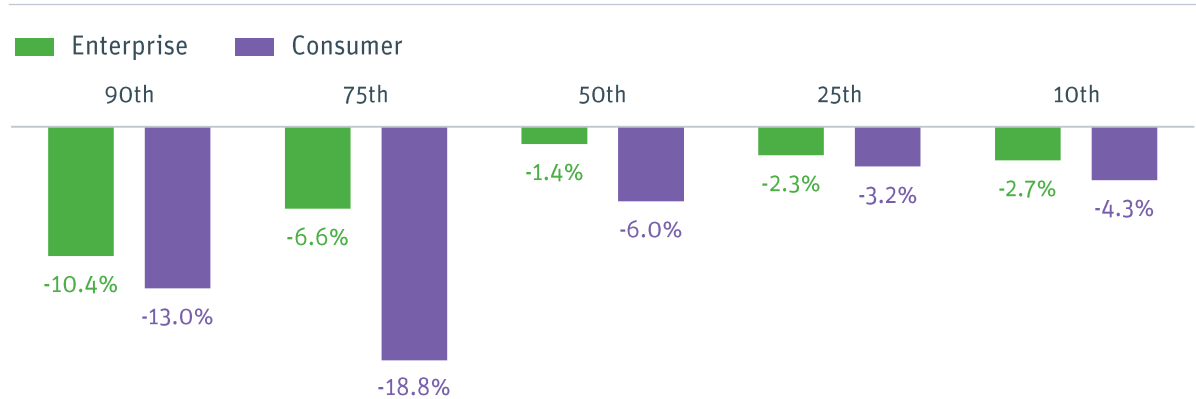
Aggregate Post-Valuation: 10 Highest-Valued Deals



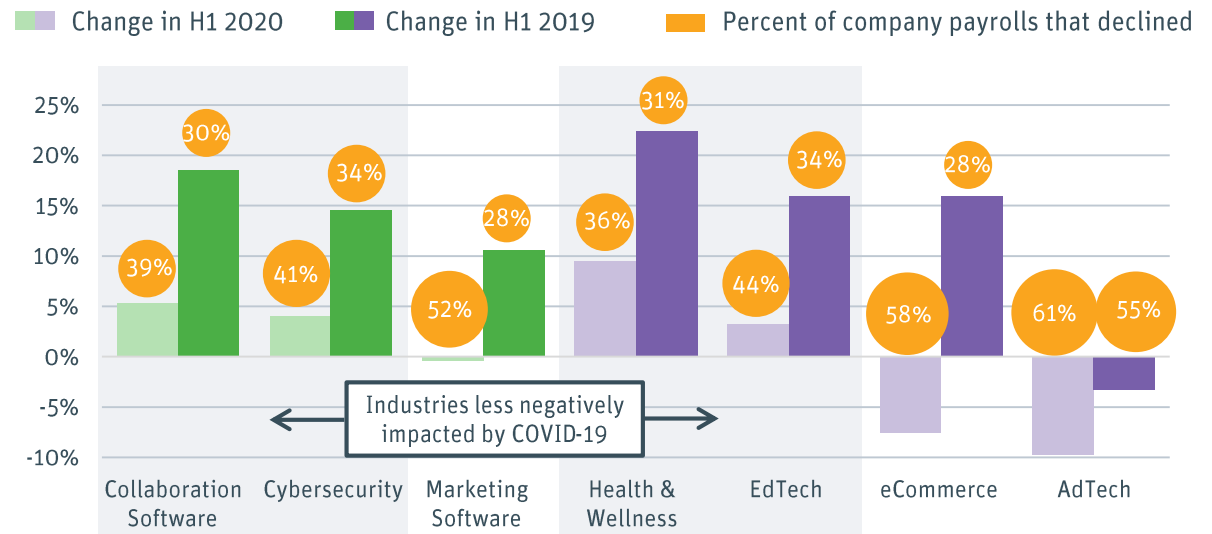
Payrolls Pressured

With revenues facing headwinds and amidst encouragement from investors, executives are taking a closer look at what expenses can be cut. Consequently, payrolls have started to fall. This decline is more pronounced for companies in the upper quartile of payroll expenses, likely as inflated salaries get pared back and workers are laid off. When broken out by SVB verticals, those companies that have benefitted from the new ways in which we work and live, have seen a smaller dip in payrolls vs. those that have been disproportionately impacted by the current pandemic.

H1 2020 Change in Payroll Expense by Expense Percentile



Change in Median Payroll Expenses¹ by Select SVB Verticals

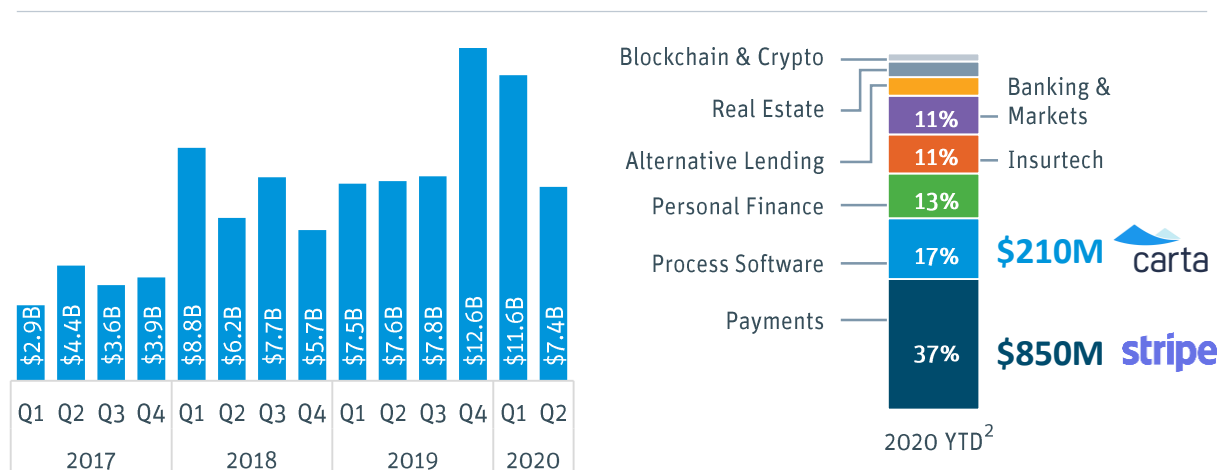


Resilient Sectors

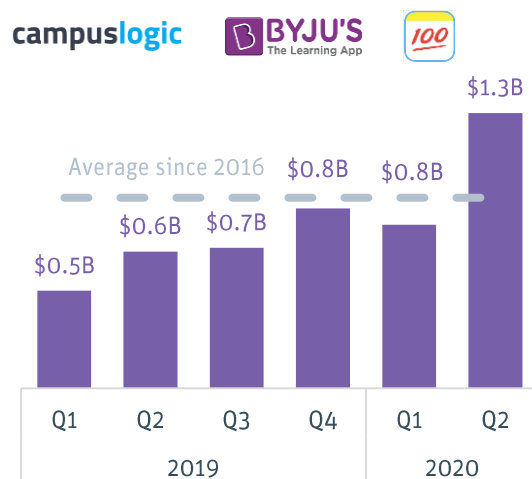
Some sectors have shown remarkable resilience during the pandemic. EdTech has seen a sharp spike in investment as much of the world adjusts to remote education. Other sectors, such as FinTech, have been resilient though not record-setting, in spite of the Great Lockdown. FinTech companies may be benefitting from forced financial digitization, though there have also been notable high-profile layoffs in the sector

The Biopharma companies that have raised this year include those working on treatments or vaccines for COVID-19 (such as Atea Pharmaceuticals), helping this sector maintain a healthy dose of funding.

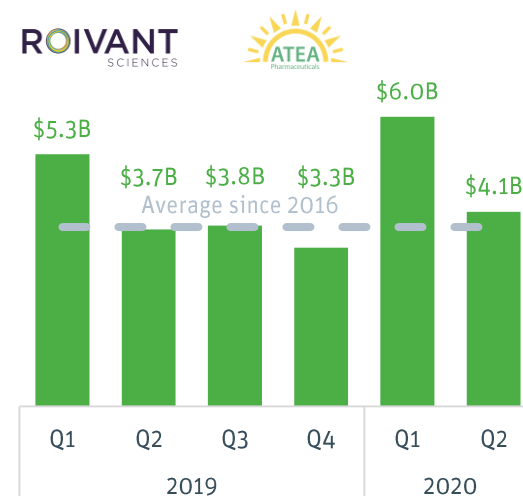
FinTech VC Investment¹ by SVB Vertical



EdTech VC Investment



Biopharma VC Investment



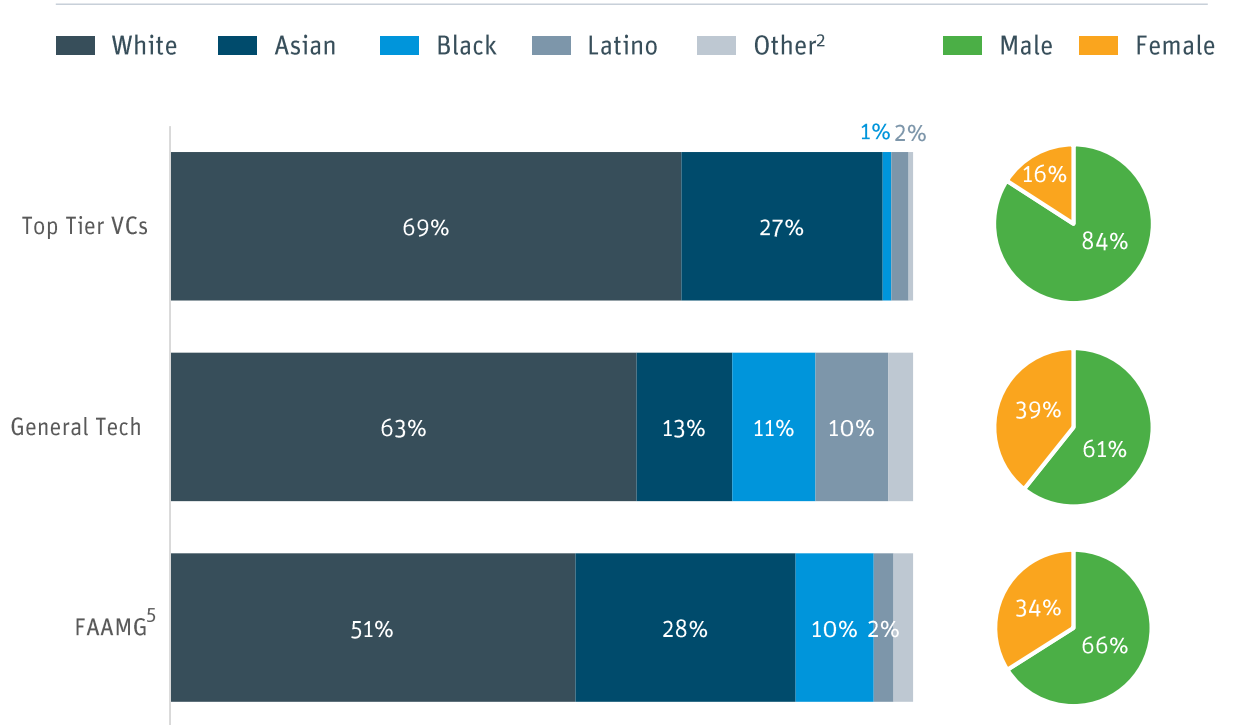
Spotlight

Social Impact

Diversity by the Numbers

Companies with above-average diversity scores for leadership report 19 percentage points more revenue coming from innovation⁴, compared to those with below-average scores. Yet the innovation economy does not reflect the diversity of the U.S., and top-tier VC firm diversity is behind the rest of the innovation economy with 16% female, 2% Latino, and 1% Black representation. Given the centrality of fundraising to the success of a young company, these numbers stack the odds against underrepresented founders.

Measures of Racial and Gender Diversity¹



- 1%** of founders are Black
- 7%** of VC firms³ have at least one Black investment professional
- 56%** of VC firms³ have only white and Asian investment professionals
- 25%** of VC firms³ have all white investment professionals

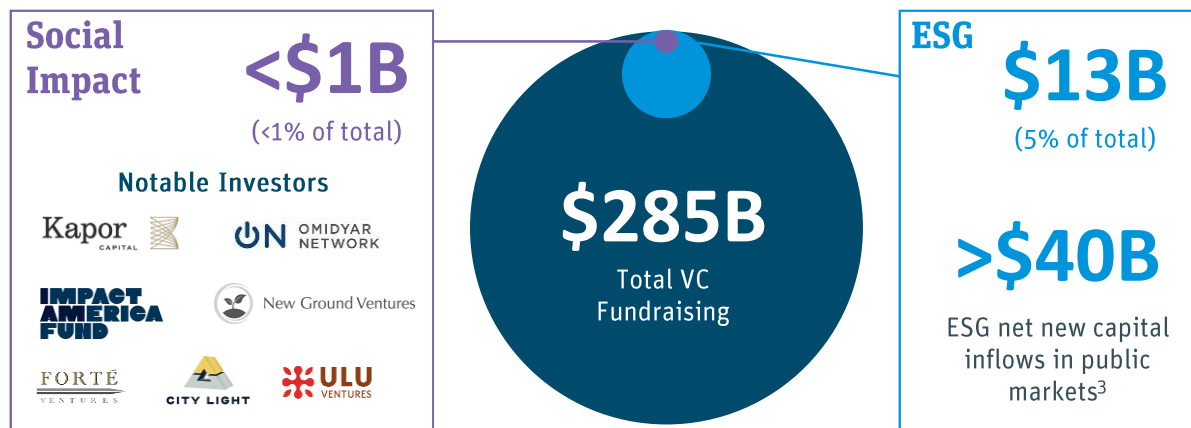
Note: 1) Races reported on most recent, publicly available EEO filing. 2) Other includes two or more races, American Indian and Hawaiian. 3) U.S.-based, active firms with at least \$250M that have made series A and B investments. 4) Products or services developed within the last two years. 5) Facebook, Amazon, Apple, Microsoft and Google (Alphabet).
Source: BCG, U.S. Equal Employment Opportunity Commission, The Information and SVB analysis.

LPs Behind on ESG, For Now

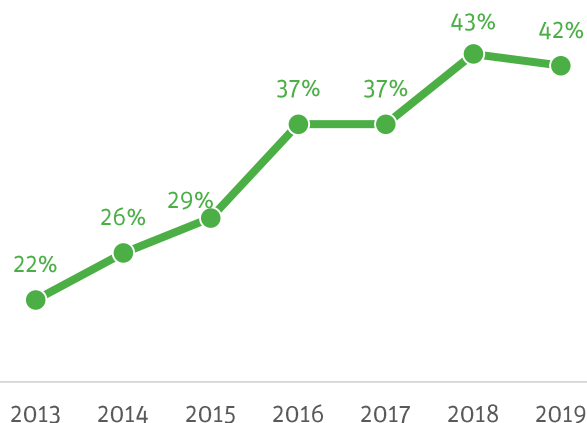
U.S. VC fundraising has boomed with more than \$285B raised since 2015. Yet a mere \$13B of that was earmarked for ESG¹. Within that bucket, less than \$1B had a social impact focus. New ESG capital inflows into public markets reached a new high of more than \$20B in 2019. As millennials continue to gain wealth and influence, ESG allocation will continue to grow.

Essentially, an explosion of interest in ESG values is yet to be meaningfully realized in the private markets. Given the zeitgeist, we expect additional allocations for ESG and social impact venture capital.

U.S. ESG¹ and Social Impact VC Fundraising (2015-H1 2020)



Share of Institutional Investors Incorporating ESG²



Startups for Social Impact



Clarity builds software that aggregates social and environmental impact data about public markets, specifically for investors.



Power to Fly is a recruiting platform designed to support women looking for companies that value diversity and inclusion.



CrowdJustice works to democratize access to the legal system, helping social impact causes via litigation crowdfunding.

Exits

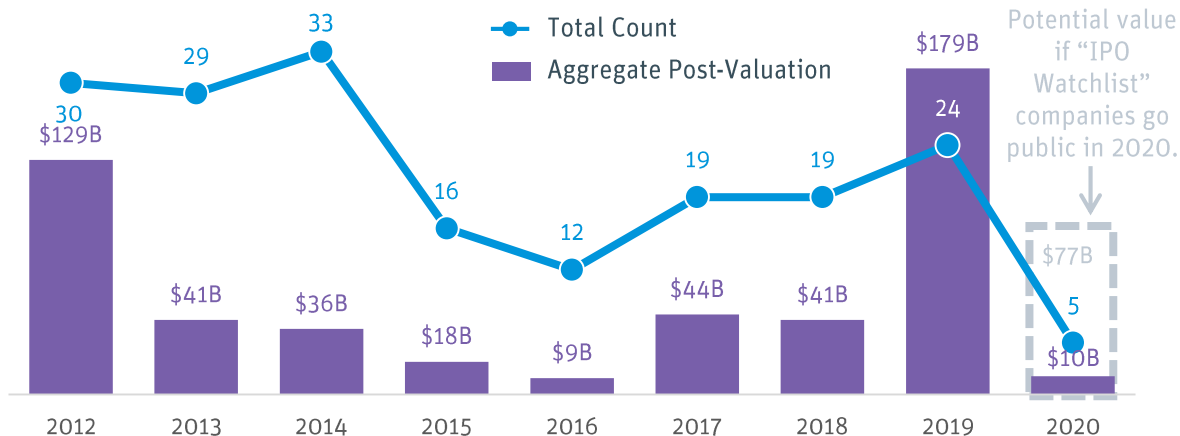
Open
Windows?



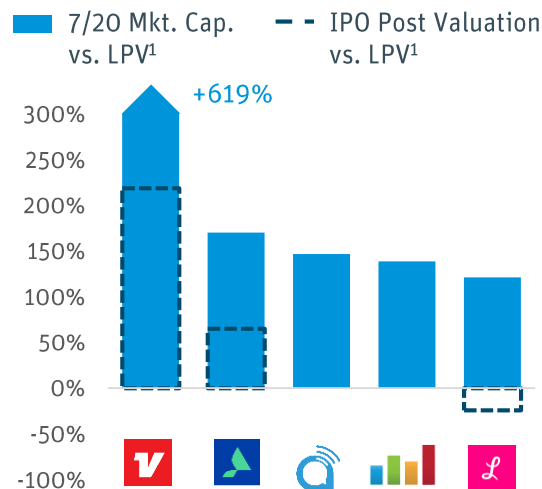
IPO Window Cracks Open

The tech IPO window effectively shut in February, as COVID-19 quickly went from a health crisis to an economic crisis, spooking investors and causing companies to put exit plans on hold. Despite volatility in the markets, we've recently seen a reemergence of VC-backed tech IPOs — with most experiencing strong returns compared to their last private valuation (LPV). Additionally, as markets have bounced back and investors' confidence has crept up, several companies are reportedly planning to go public in H2 2020, which could put this year's aggregate valuation in the top three for the last decade and set a record for direct listings.

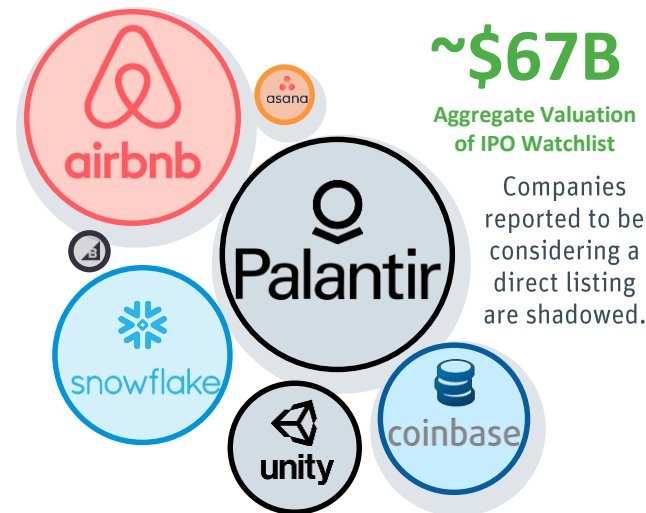
U.S. VC-Backed Tech IPOs: Count and Post-Valuation



Performance vs. LPV¹



IPO Watchlist²

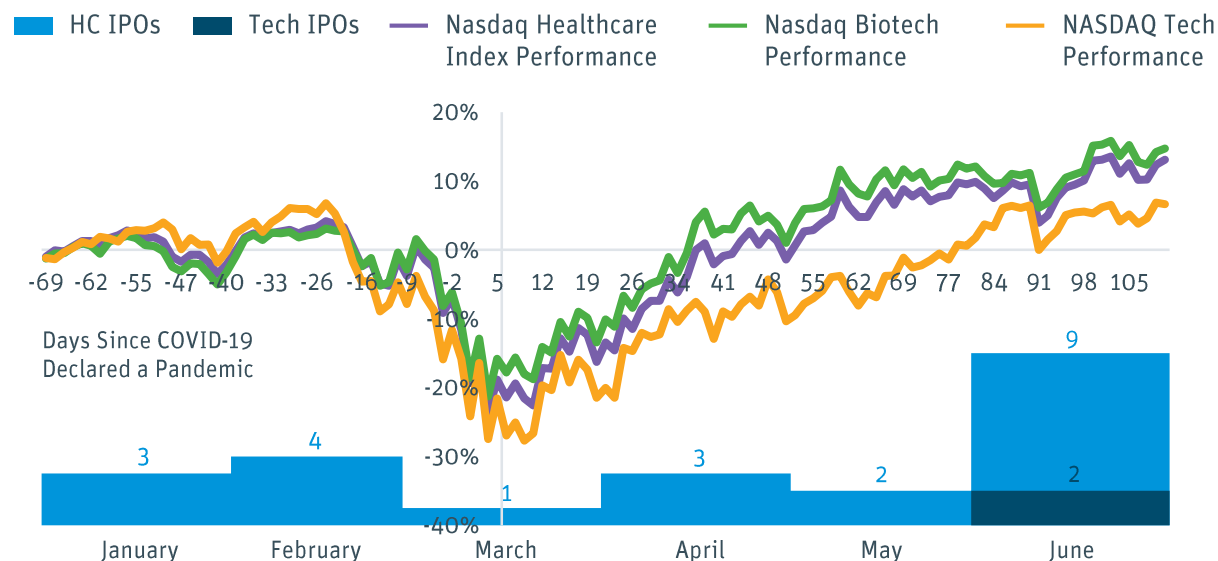


The IPO Window Never Closed for Healthcare

While the COVID-19 pandemic has resulted in multiple tech IPOs being pushed back to H2 2020 or later, healthcare IPOs have continued. These offerings are overwhelmingly by Biopharma companies, which comprise 17 of the 22 U.S. healthcare companies that have listed on the Nasdaq this year.

SVB tracks the top 15 crossover-backed mezzanine deals (\$40M+) as a proxy for IPO sentiment and pipeline. In H1 2020, 34 qualified for the list and four have already gone public².

Nasdaq Healthcare vs. Tech Performance¹



Notable 2020 Healthcare IPOs²

	SVB Healthcare Sector	IPO Price (Date)	Price 07/14/20	Price +/-	Market Cap 07/14/20
SCHRODINGER	Dx/Tools or HealthTech	\$17.00 (2/6/20)	\$82.63	+386%	\$5.2B
LEGEND BIOTECH	Biopharma	\$23.00 (06/05/20)	\$37.47	+63%	\$4.9B
one medical	HealthTech	\$14.00 (1/30/20)	\$37.75	+170%	\$4.8B
INARI MEDICAL	Device	\$19.00 (5/22/20)	\$51.41	+171%	\$2.5B

Notes: 1) As of 7/14/2020. 2) Companies with a \$2.5B+ Market Cap that went public in H1 2020 are shown. For a full analysis of healthcare exits, see SVB's Mid-Year Report. Schrodinger is classified as both a dx/tools and healthtech company and is counted as a healthtech company for the total IPOs. Source: S&P Capital IQ, PitchBook and SVB analysis.

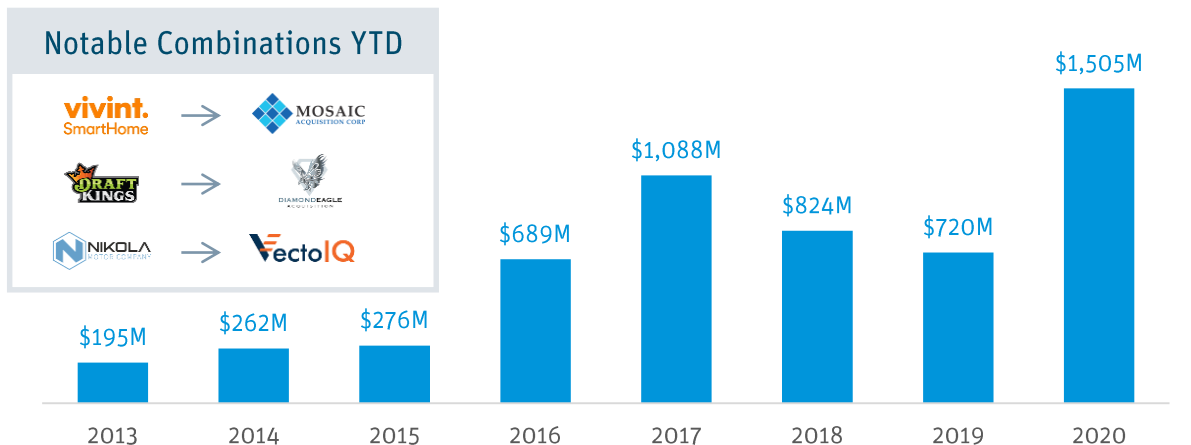
Return of the SPAC

This year has seen a meteoric rise in SPACs¹. For innovation companies, they have emerged as a realistic alternative to an IPO, providing an advantage in terms of flexibility and speed. In 2020 alone, SPACs have accounted for roughly 35% of U.S. IPO filings and are only getting bigger—highlighted by Bill Ackman’s recent SPAC IPO, which raised \$4B, becoming the largest SPAC IPO ever. Notable companies have been acquired by a SPAC this year, with more in the pipeline including Fisker and Multiplan—the latter being the biggest SPAC merger ever. If SPACs and direct listings continue to gain adoption, the traditional IPO route could eventually become antiquated.

U.S. SPAC IPO Count and Amount Raised by Year²



Average SPAC Deal Merger Size³



Notable Combinations YTD

- vivint. SmartHome → MOSAIC ACQUISITION CORP.
- DRAFT KINGS → DIAMONDEAGLE ACQUISITION
- NIKOLA → VectoIQ

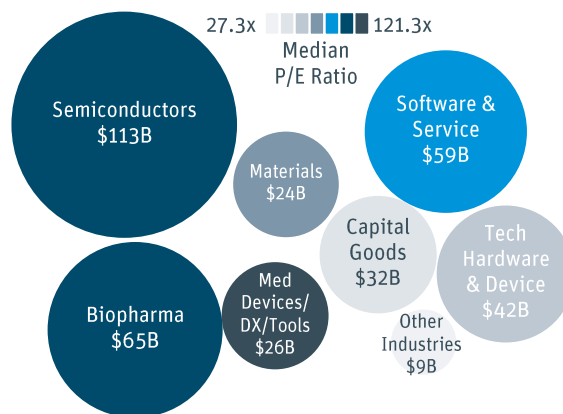
International Global Ecosystems Evolving

The STAR Experiment, One Year In

The STAR¹ Market represents China's answer to the Nasdaq; its mission is to attract innovative companies in China and greater Asia to go public in Shanghai.

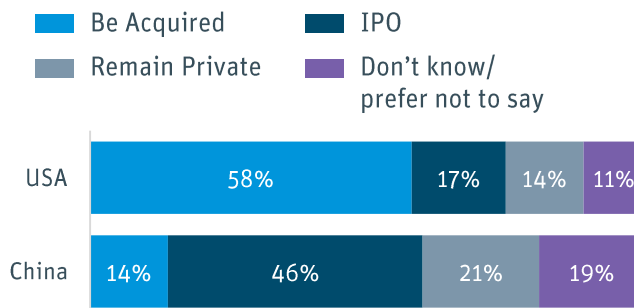
After one year, the STAR market has become the venue for many of the largest IPOs by Chinese tech companies, attracted in part by frothy trading multiples and lenient profitability standards. The presence of this tech-focused market amidst trade tensions and decoupling may further reinforce the higher preference to go public among Chinese entrepreneurs versus Americans, evidenced by SVB survey results.

Industry Aggregate Market Cap, STAR-Listed Companies²

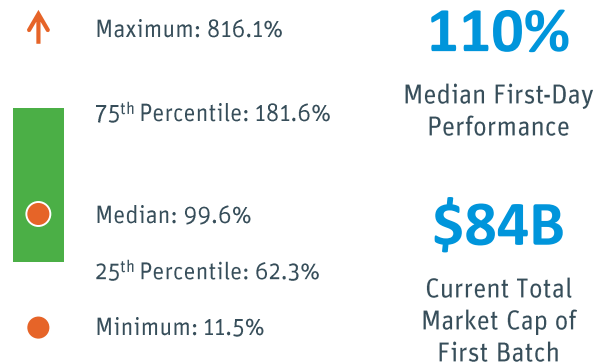


SVB Startup Outlook Survey

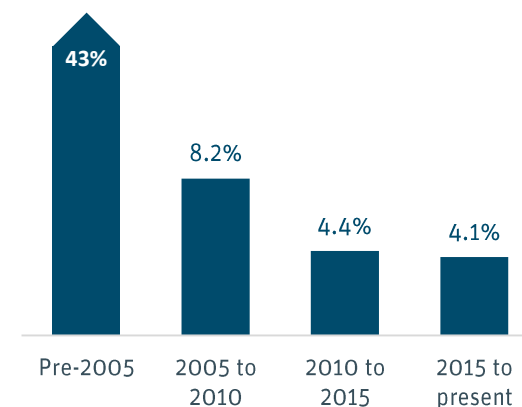
What is the realistic long-term goal for your company?



Performance Since IPO, STAR Market First Batch³



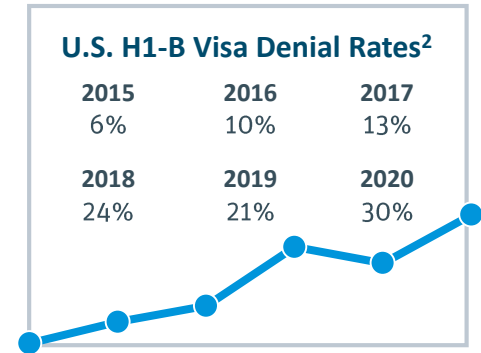
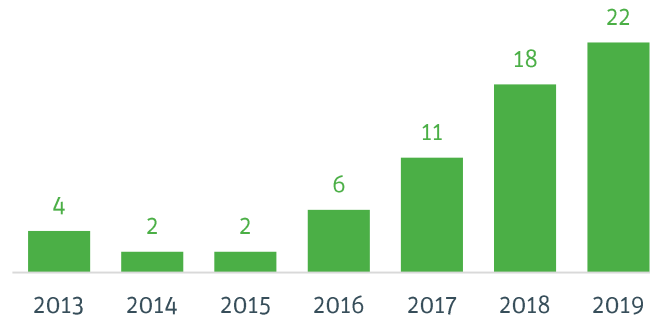
Nasdaq Share of Chinese Tech IPOs



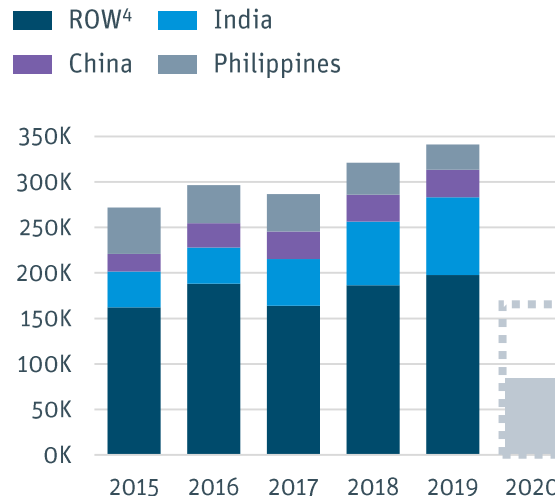
Canada Taps Tech Talent

Canada has been able to attract and nurture some of the strongest tech talent in the world due to its friendly immigration policies and world-class universities. This trend has only accelerated with the U.S. toughening its immigration stance — causing a spike in denial rates of H1-B visas (work permits for highly skilled workers) and companies opening offices in Canada to gain access to talent. Canada has pledged to increase the number of immigrants it accepts each year by 40,000, aiming for 350,000 in 2021. It has also implemented the Start-up Visa Program and Global Skills Strategy (GSS).

Silicon Valley Tech Companies¹ Opening Offices in Canada



Admission of Permanent Residents by Country



GSS³ Program Highlights

2 weeks

Processing time for application to be approved.

5x

Number of successful applicants to Canada's GSS program rose five-fold over its first three years.

62%

Citizens of India accounted for 62% of successful applicants to program, followed by citizens of China.

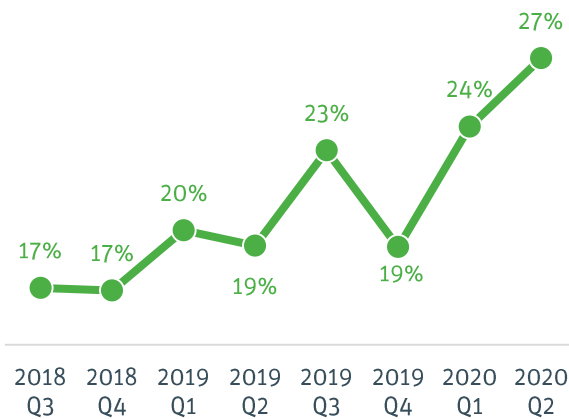
23,000+

Workers approved under the top 5 tech categories, with 2,300+ being approved in the first 3 months of 2020.

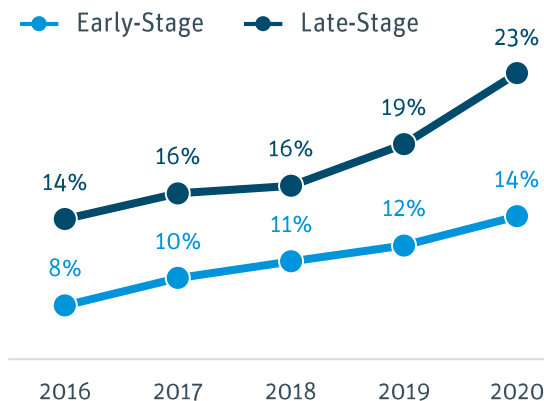
FinTech Shines in Late-Stage Boom

As in the U.S., the late-stage ecosystem in Europe has taken a larger share of deals, increasing eight percentage points through H1 2020. The share of late-stage deals with at least one U.S. investor has increased four percentage points over 2019, illustrating U.S. investor appetite for European companies and continued cross-border investment, despite travel restrictions. FinTech has not only capitalized on the growing share of late-stage deals, but has leveraged the COVID-induced transition to online payments and banking as a way to gain new users who were initially reluctant to adopt online banking.

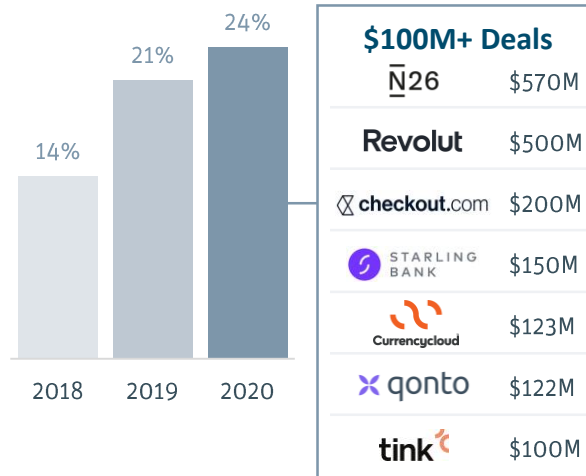
Late-Stage Share of Tech Deals (Europe)



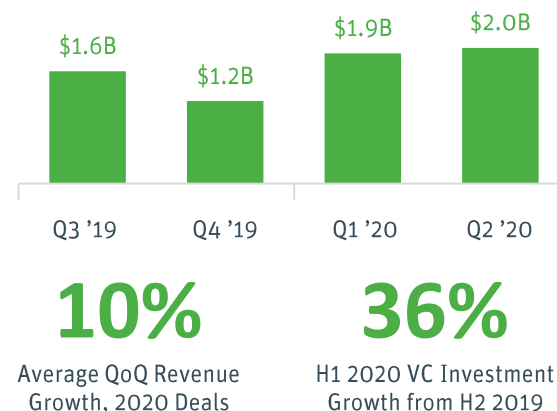
Percent of European VC Deals with a U.S. Investor



Share of Late-Stage Capital Going to FinTech (Europe)



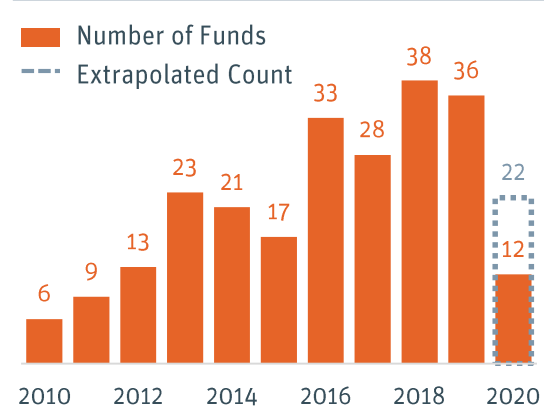
Investment in European FinTech



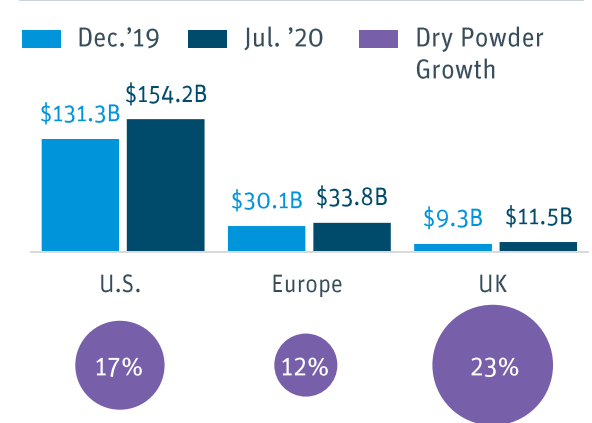
Dry Powder Expands, Bound for Europe

H1 2020 has seen strong fundraising, with dry powder increasing in both U.S. and European markets. The U.S. has seen the first signs of a slowdown in fundraising, with the average fund closing at 84% of its target in 2020. However, in Europe, the average fund closed at 105% of its target, suggesting stronger fundraising dynamics. Given the long duration of fundraising cycles, we will likely see a modest slowdown late in 2020, but low interest rates across the globe and volatile public markets should buoy private fundraising.

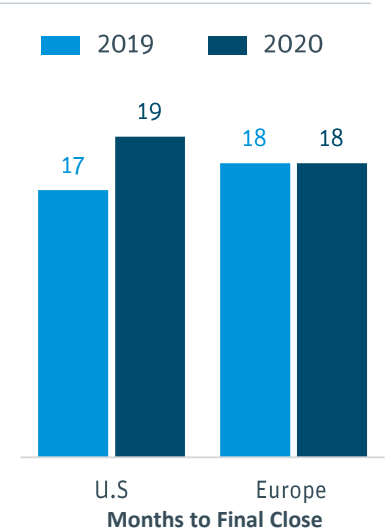
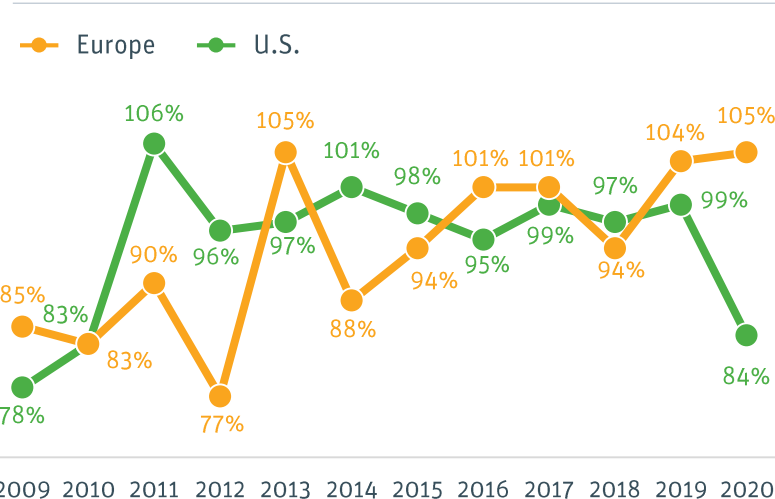
U.S. HQ Funds with European Focus by Vintage Year



VC Dry Powder Growth



VC Funds: Percentage of Target Size Secured U.S. vs. Europe



Appendix

Report Authors



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Bob Blee heads Silicon Valley Bank's Corporate Finance Group, which leads SVB's relationships with public and late-stage private companies in the Innovation sector throughout North America, providing a full suite of lending and banking products, and guidance as a trusted partner, helping our clients succeed and quickly scale.

Previously, Bob held a variety of roles in SVB's California and Midwest regions, including heading seed, early and mid-stage Infrastructure, Hardware and Consumer Internet and FinTech banking in the Bay Area and Southern California and was responsible for SVB's Mezzanine Lending and Loan Syndications practices.

Bob sits on the nonprofit board of the Network for Teaching Entrepreneurship (NFTE) and the Silicon Valley Advisory Council of the Commonwealth Club. He is also active with his alma mater, the University of Illinois.



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