Capital Provider Market Sentiment Survey

Conducted by Bigfoot Capital

June/July 2022

Survey Purpose

Gather quantitative and qualitative data from early/growth stage equity and debt investors on:

1. Their market sentiment
2. How they may shift their strategies
3. What it means for their investing activity

Top Takeaways

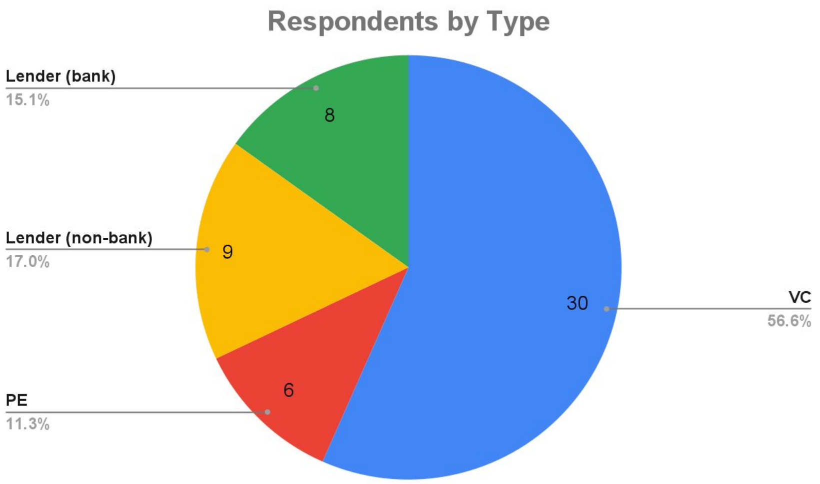
- **Sentiment** - While 90% of respondents believe a **recession is coming** in the next 12 months, there's not as much negativity as one may expect. Banks are the most negative, Seed/A investors are the most positive and there's a healthy dose of neutrality (understandable given the uncertainty). Equity investors are breathing a sigh of relief with an anticipated **valuation reset** across stages and lenders (along with equity investors) are focused on quality over growth (a marked shift from the past few years).

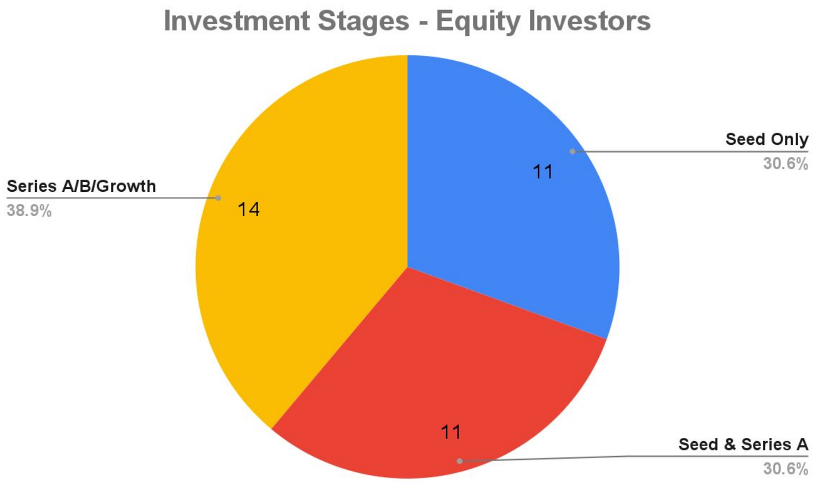
- **Strategy** - Only 10% of "Seed Only" VCs indicated a shift in strategy while 40-50% of Seed/A VC, A/B/Growth VC and PE and non-bank lenders indicated some shift. Themes emerged around raising of the bar for investability, more thoughtful deployment, more **discipline** and a return to focus on **fundamentals**. Everyone seems quite **burn wary**.

- **Activity** - It's quite interesting that with an anticipated recession 60% of this brave group of individuals reported they will **increase their investment activity** over the next 12 months. This holds across equity and debt deploying at all stages within B2B. It seems this is an opportunistic bunch with capital to deploy, conviction in their approaches and quite a bit of **excitement to pursue quality assets at more reasonable prices**. Additionally, 60% of equity respondents reported they **expect up to 25% of portfolio companies to need bridge financing** in the next 12 months. They've all (but 1) indicated they'll step up and almost half of them will look to lenders to play a role too.

The Participants

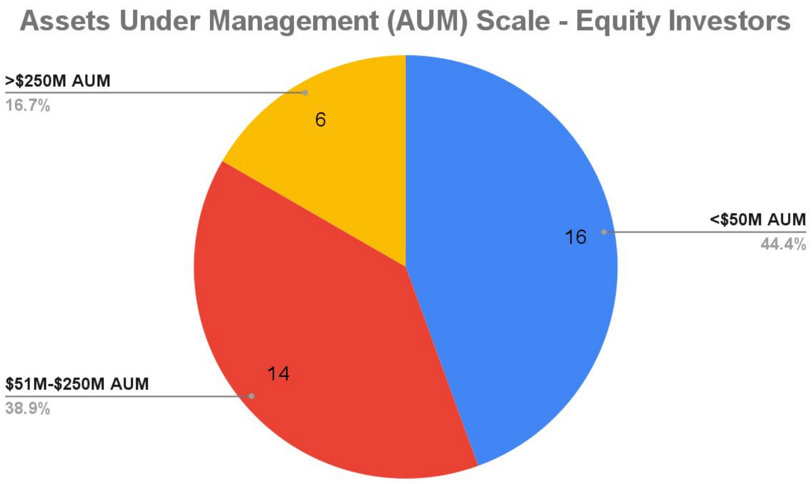
53 capital providers shared their thoughts, split as follows

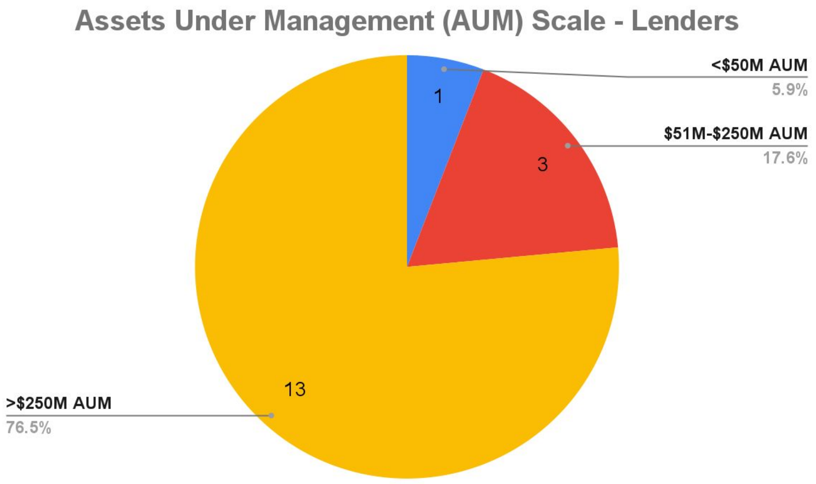




Respondents are 68% equity / 32% debt. 96% primarily focused on B2B. Pretty equal weighted across stages.

Respondents by Assets Under Management (AUM)





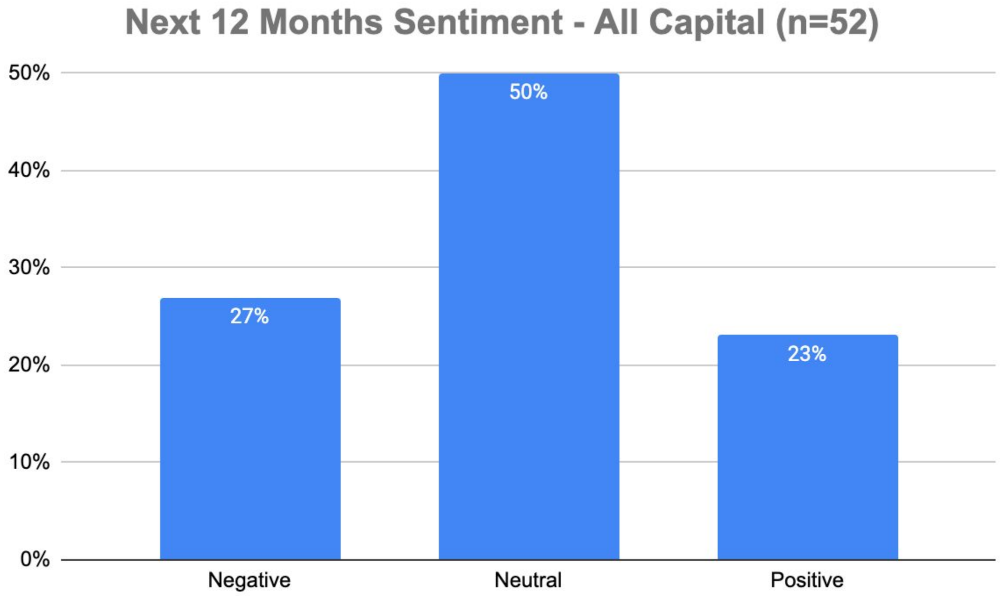
~80% of equity investors <$250M AUM, ~80% of lenders >$250 AUM

Market Sentiment

91% of survey respondents believe a recession is coming in the next 12 months

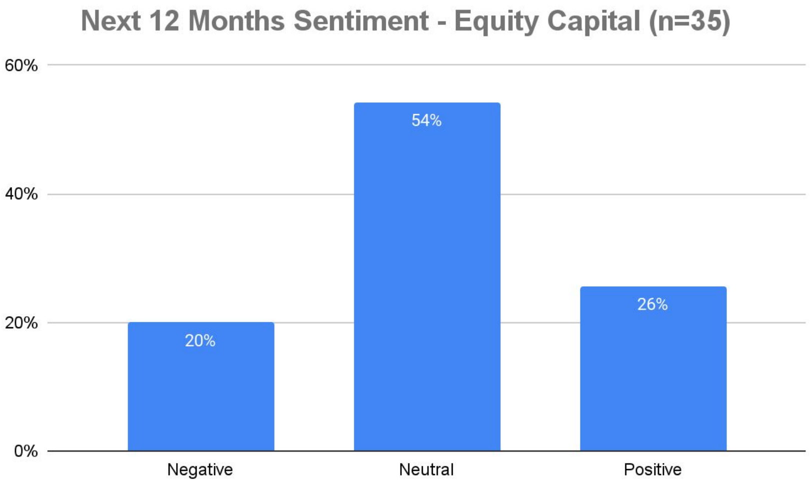
With that said, let's see how everyone's actually feeling

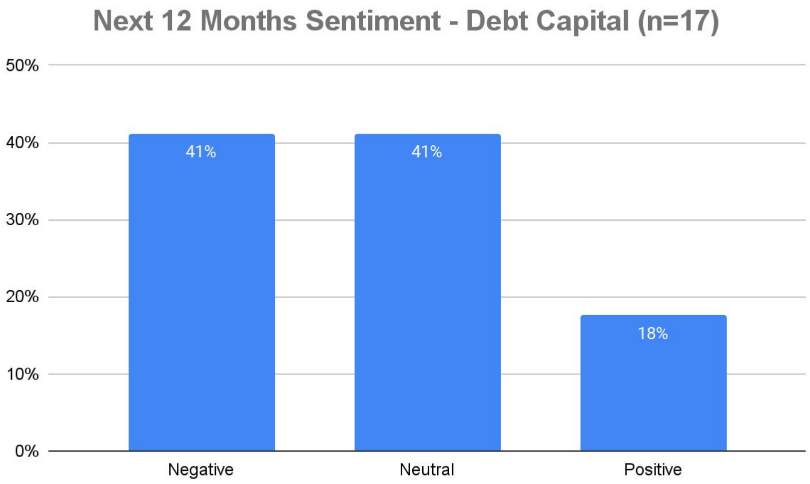
So, how's everyone feeling?



Pretty ok I guess…with some segmenting, the results get a bit more informative.

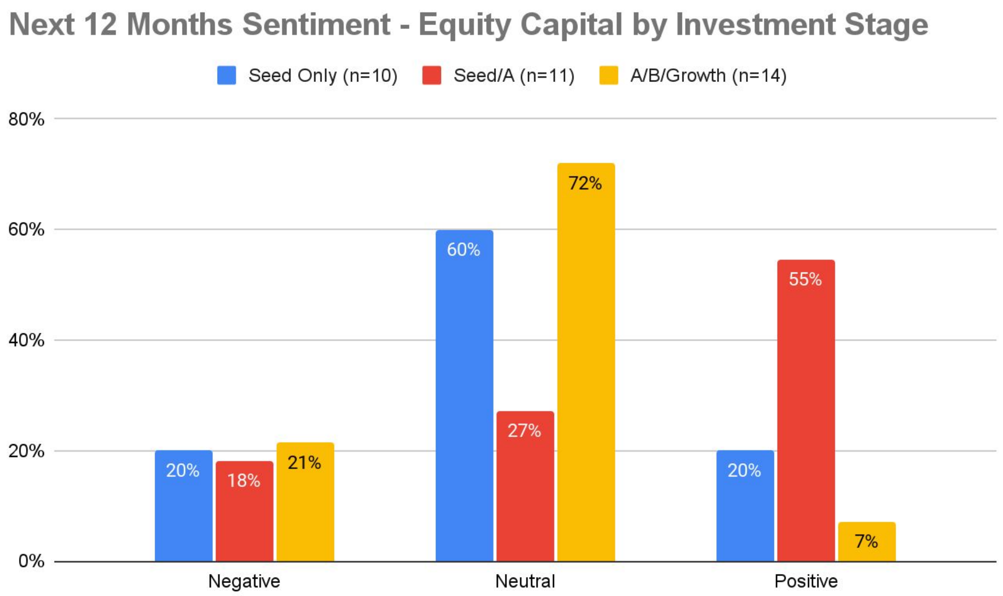
Sentiment - All surveyed capital providers





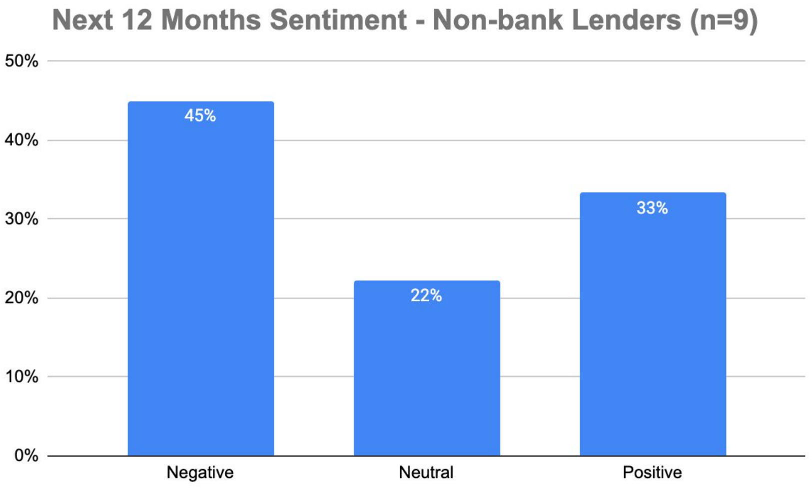
Equity pretty split. Debt more decisively neutral/negative (it doesn't make us bad people).

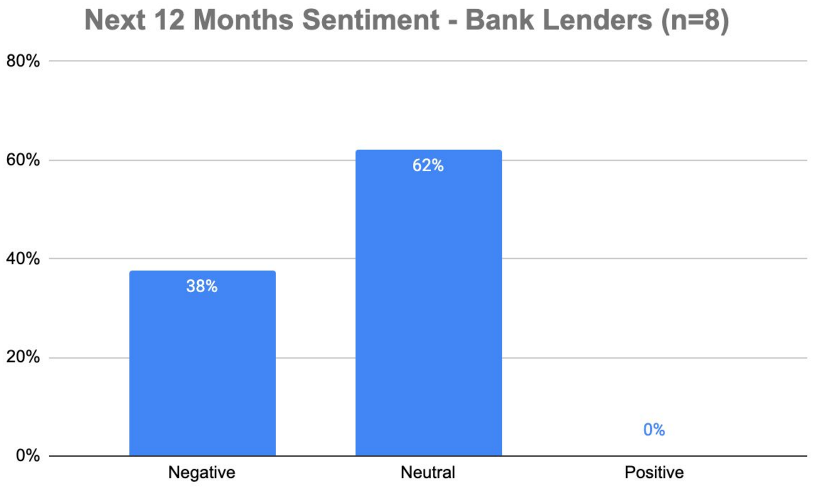
Sentiment - Equity capital providers by stage



Seed/A is pumped! Seed only is undecided. Growth is neutral/negative. Lenders?

Sentiment - Debt capital providers by type





Non-banks have a slight positive skew. Banks showing **0** positivity. *Realize the sample is quite small, but still*

Seed Only VCs Said

- "Still very overvalued - plenty of room down, a necessary down cycle"
- "2021 valuations were unsustainable. This market shakeout is healthy for VC market long-term"
- "I expect new investment valuations to drop: 50%+ for growth rounds, 25% for Seed and Series A"
- "Those with discipline and fundamentals are not directly impacted but will get caught as collateral damage as those who lost them aim to rediscover them"
- "Bad news - interest rates rising, exit values declining, general hesitation among investors. Good news - valuations are correcting, companies are more thoughtful about their burn rates"

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Seed Only VCs (also) Said

- “Not worried about finding investments to fill out portfolio and will likely see better pricing. Worry a little more about sales velocity of existing companies and their ability to raise capital or get to good exit values. Worry most about raising next fund as LPs are all over allocated to private markets”

- “2020 VCs went from investment businesses to "asset preservation businesses". 2021/early 2022 VCs needed to catch up for a lost year, leading to inflated valuations and larger capital raises. Now that investors have caught up, combined with compressed valuations in the public and late growth stage markets, there is less urgency to do deals and lower valuations downstream.”

Seed/A VCs Said

- “Volatile. Correction. Opportunity.”
- “Our hope is that good business fundamentals will prevail and over capitalized over valued companies will be forced to reset back down to earth”
- “I believe this is a return to a sober valuation environment and a much needed correction given the recent market run. This will create opportunities for us at the seed+ stage where more companies will opt to raise seed extensions versus a larger Series A”
- “A return to norm/air coming out of bubble”
- “More panic than necessary”
- “It was a much needed correction to rounds that were too big and valuations that were too high”

A/B/Growth Equity Said

- "Overcorrection of a market that never properly reflected the impacts of the pandemic and civil unrest"
- "Recession coming, back to earth for SaaS valuations, buying time"
- "We expect a flight to profitable businesses. Those with large burn rates will struggle to raise capital"
- **Next wave of concern:** "The real problem comes if/when businesses meaningfully slow IT spend."
- "We are more value based buyers and investors, so we are looking forward to asset prices normalizing a bit. Our investment horizons are long enough that we are not concerned about a pull back in asset prices, especially in the context of the two-year run-up"

A/B/Growth Equity (also) Said

- "A valuation reset was much needed in Series A and B, and recessions provide for incredible investment vintages, so I am optimistic about the opportunities coming up in the next 12 mo"
- "I'm finding that a lot of prospects are delaying their raises. Because we lean more growth equity and capital efficient, most of the companies are in decent shape. Raising or running a process for liquidity for them isn't a huge priority, so they are tending to wait it out until later in 2022. I think that opens up debt as a bridge option if they do want to take advantage of hiring someone now"

Non-bank Lenders Said

- “Valuations coming down to more rational levels but not tanking to recession levels”
- “Many entrepreneurs have not accepted that their company is worth less than it was 6 months ago”
- “Great opportunity for established, experienced lenders with dry powder! Tourist money is fleeing”
- “Pessimism has kicked in and will remain into '23”
- “Macro risk for asset sensitive business models, hiring pull back for software to impact growth, valuation uncertainty caused by public equity volatility causing pause and slow down in venture”
- “CFBE or positive companies will be fine but burning companies will have challenges raising capital. Revenue growth across the board likely comes down for the next 12 to 24 months”
- **Our Personal Favorite:** “The drunker you get, the worse the hangover. Everyone was VERY drunk the last few years”

Bankers Said

- "RIP the good times. We're focused on companies who are investable and being wary of companies who may face a down round for the fundraising cycle"
- "We are being more diligent on supply chain and employee risks along with interest rate sensitivity analysis, given rates will continue to climb in the next 12 months"
- "Inflation, supply chain disruptions, employee shortages and negative consumer sentiment will lead to a recession in the next 12 months"
- "In a bad place, current administration has totally screwed up the economy"
- "Multiples have come down significantly on LBOs on the ARR side, but on the cash flow side, companies appear to still be getting what they want. The very real impact of loosey goosey fiscal policy and irresponsible spending and printing has led to inflation beyond anyone's belief. Will see how things shake out but overall I think the tech sector should hold up as it always has"
- **Words to take to heart:** "Free money is never free"

Strategy Shifts

Seed Only VCs Said

- ~10% said no shift in strategy. The rest said:
- “Lower valuation expectations across the board (new investments and next rounds)”
- “Valuations will likely come way down, so being patient now, and waiting for better terms on new deals”
- “Keeping high bar. Entry price matters. Capital efficient founders! Do more with less”
- “I am still relatively risk-on, but am looking for more reasonable entry valuation in the current market”
- “Raise more; push your next round metrics further out; or just be profitable”
- “Reserving more capital for a more concentrated portfolio”
- “We're staying consistent through cycles as we have a long time horizon for our fund. We are getting slightly more aggressive on valuations when we can”

Seed Only VCs (also) Said

- “Trying to go at more measured pace and get more time diversity in portfolio which has been struggle past 24 months. Still plan on dozen new investments within next 18 months”
- “In some cases we're increasing investment amounts to provide longer runway, and in others we're increasing investment reserves to be able to manage bridge or follow-on rounds”

Seed/A VCs Said

- ~50% said no shift in strategy. The rest said:
- “Watch and learn. No rush to deploy, but there will be great deals and great businesses that pull through this”
- “Being more thoughtful about deploying capital”
- “Criteria is the same but more emphasis on capital efficient growth versus growth at all costs and make sure companies have 18-24 months runway”
- “Gunning hard!”

A/B/Growth Equity Said

- ~45% said no shift in strategy. The rest said:
- “We are angling slightly towards protecting cash flow, but we are still investing in our companies”
- “Higher reward for capital efficiency”
- “Refocus on price discipline and staying in our lane”
- “We're slowing investment activity to some degree and taking our time in diligence. We'll likely be more demanding on valuation and terms as well”
- “We believe there will be opportunities in our space to acquire businesses from SMB owners who may be looking to exit coming off of market issues caused by Covid-19 and staring down a potential recession”
- “No expectations to sell or raise within the portfolio for 12 months (unless emergency need)”

Non-bank Lenders Said

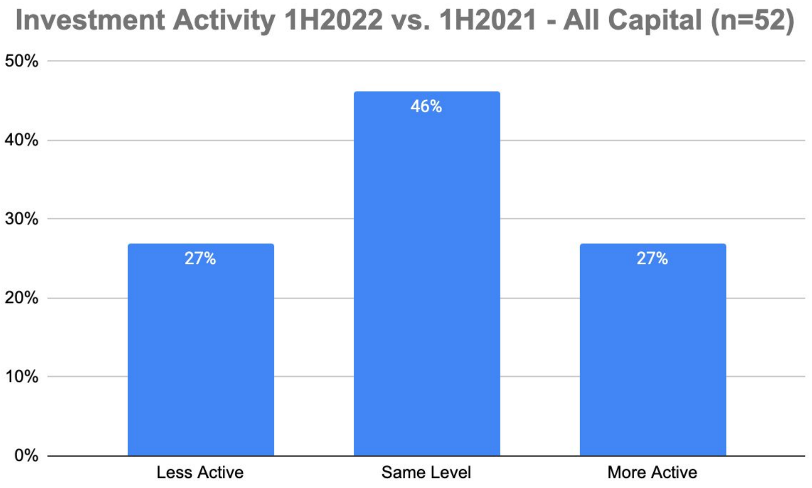
- ~40% said no shift in strategy. The rest said:
- "Just being more selective, but otherwise no big changes"
- "More sensitive to high burn growth models"
- "Shifting to CFBE or positive investments. Will selectively do cash flow negative if its high growth with a path to profitability"
- "Leaning in to quality deals, improved structure/economics"
- "Credit bar is higher. Need to see more runway, greater KPI scrutiny, view need for additional capital as much higher risk than anytime in last decade plus"

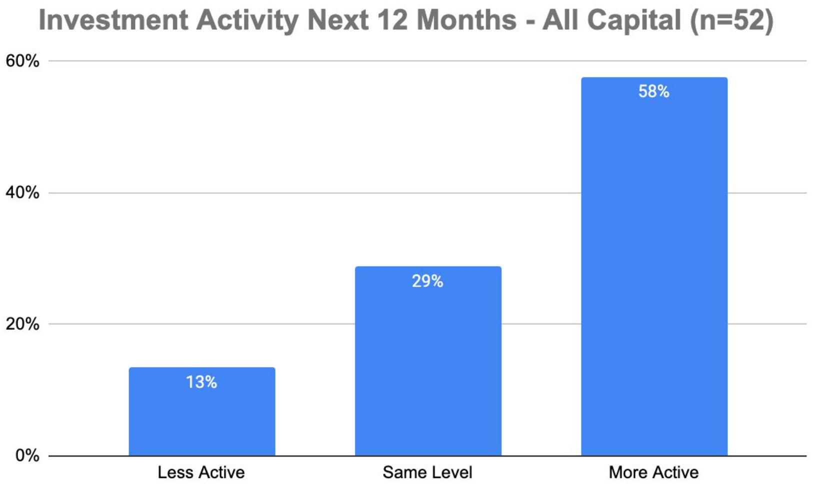
Bankers Said

- “The bank is cutting back in credit due to inflation and the impending recession”
- “Enhanced due diligence and tighter credit structures”
- “Focusing on company fundamentals including burn multiple, unit economics and strong equity sponsors”
- “Continuing to fund strong performers, strong profile companies with solid LTV. Definitely seeing a slow down in new platform investments but the pipeline remains healthy. The team will be focused on the existing portfolio and how it makes it through the next set of hikes/inflation/supply chain issues impacting all businesses and consumers”

Investing Activity

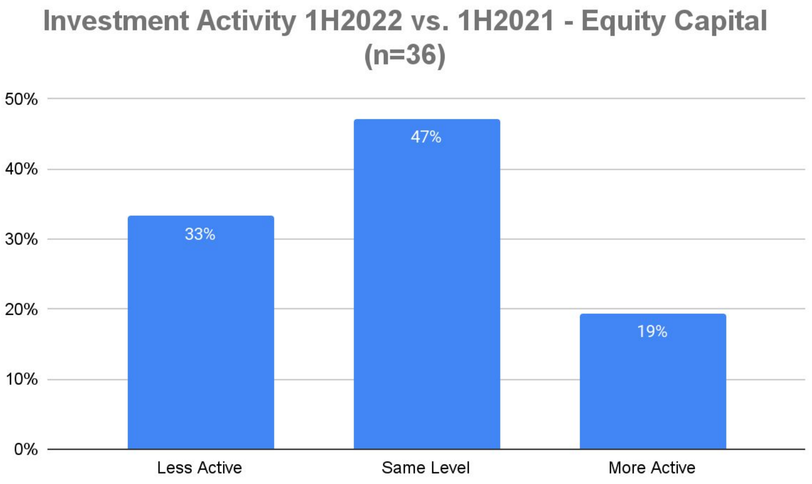
How’s everyone’s investing activity looking?

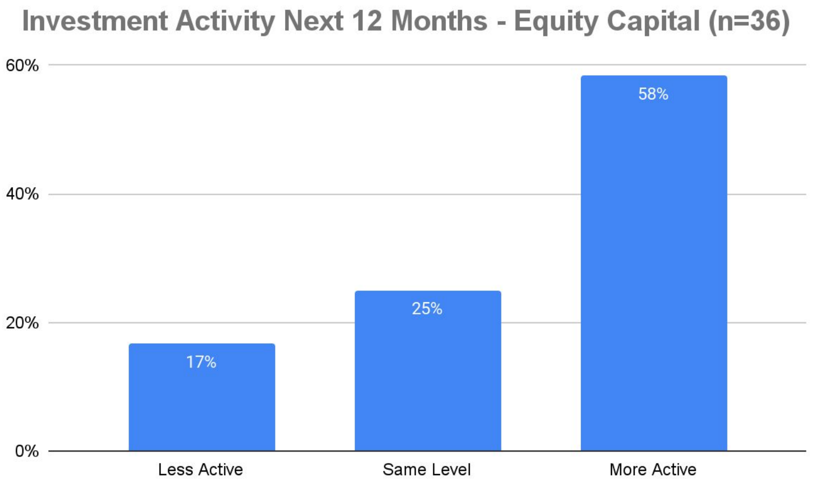




Mixed bag YTD 2022 vs. YTD 2021. A lot of folks licking their chops for the next 12 months! Let’s segment.

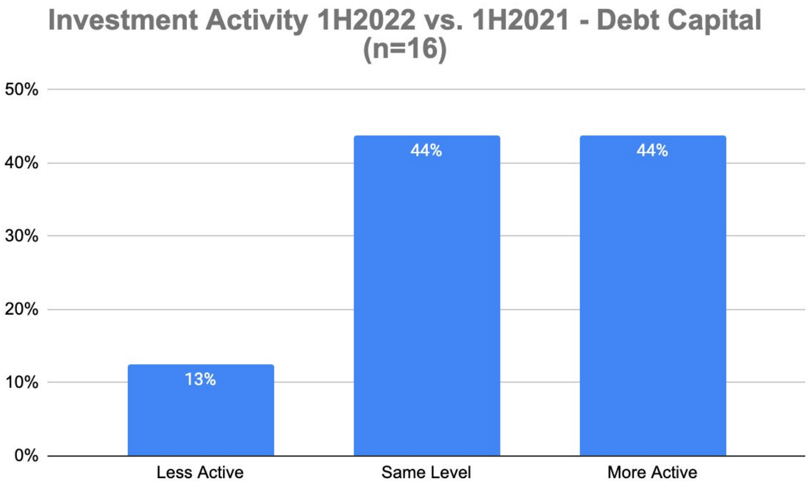
Investment Activity - All surveyed equity capital providers

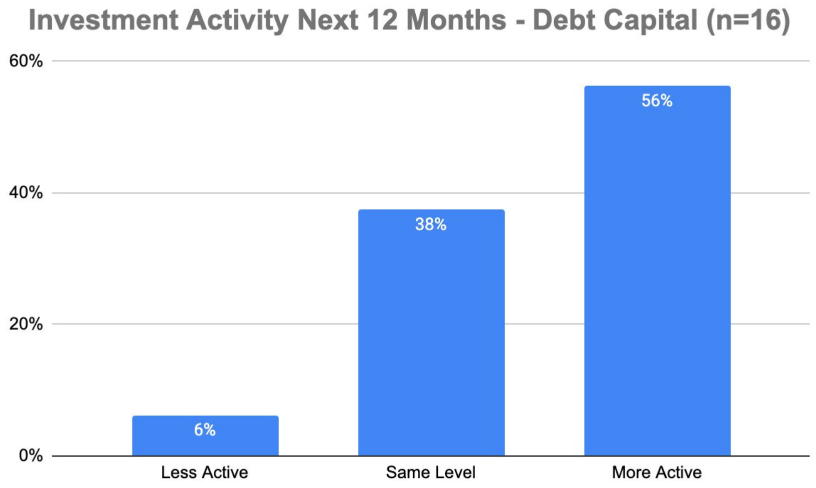




Expecting a big pendulum swing to more investment activity over the next 12 months w/ tastier valuations.

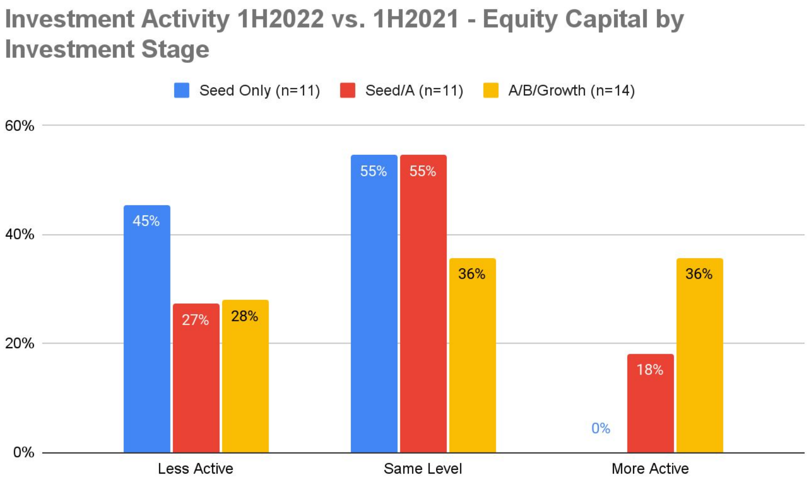
Investment Activity - All surveyed debt capital providers

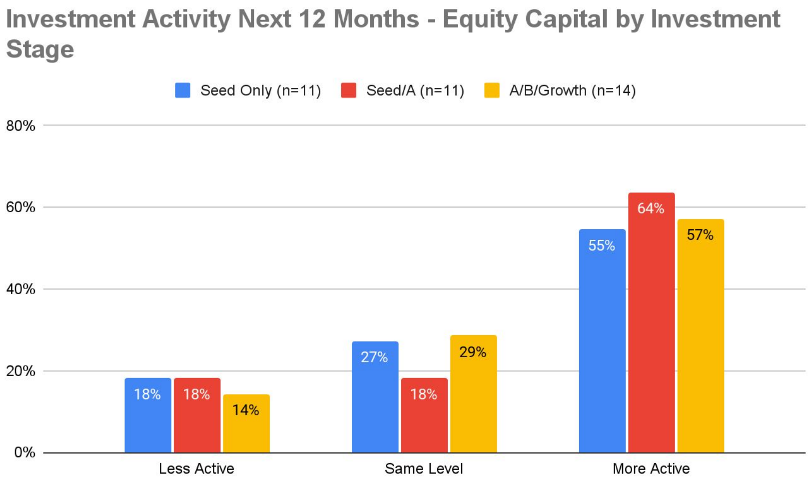




Despite it's bearish sentiment, debt has been and intends to continue to be on fire (w/ deal activity)!

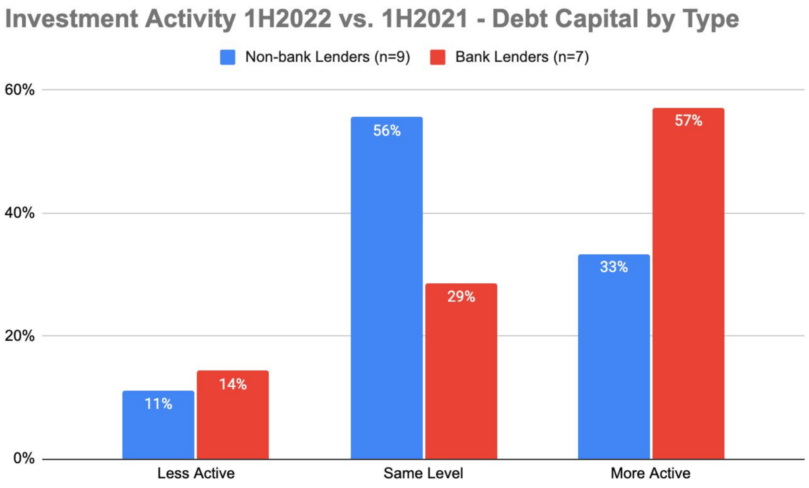
Investment Activity - Equity capital providers by stage

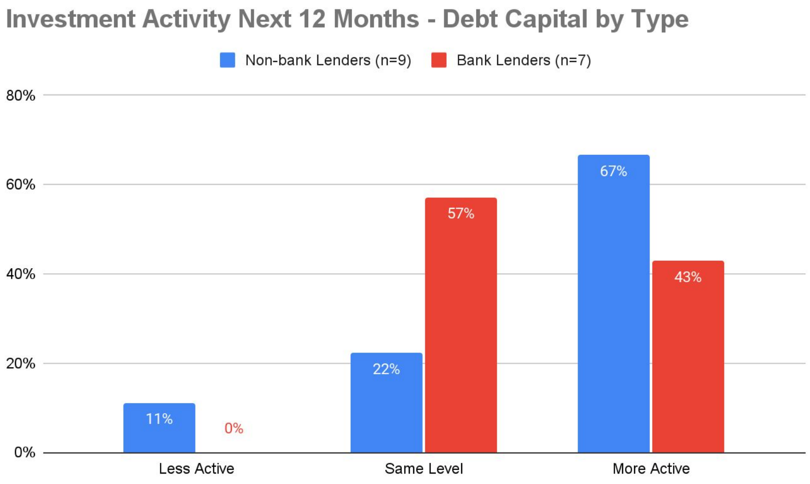




Resounding increase in investment activity across stages. Equity checks will be written!

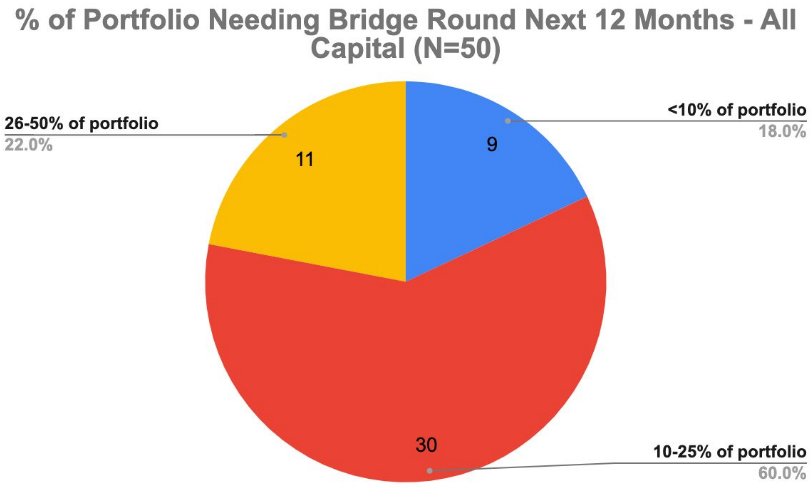
Investment Activity - Debt capital providers by type

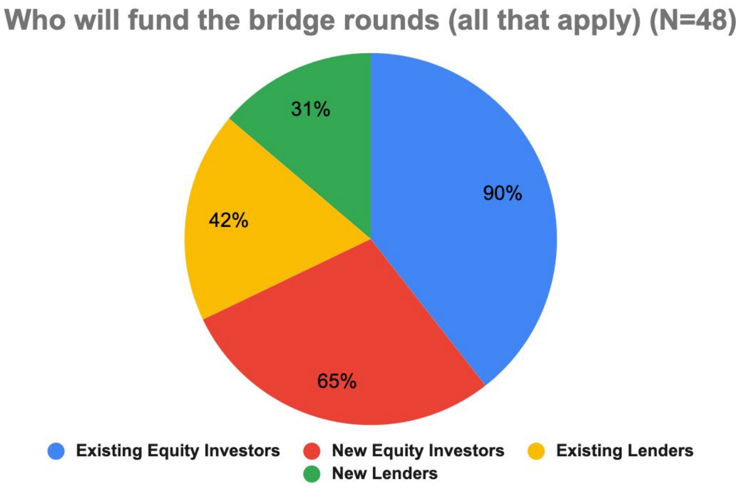




Banks have been quite active YTD (venture debt facilities being tapped). Lending capital will keep flowing.

Anticipated Bridge Financing Needs





All but 1 equity investor says they'll help bridge, 44% of equity investors are looking to lenders to help bridge, 85% of lenders are looking for the same from existing equity investors

Thanks to all contributors and readers!

If you'd like to discuss, collaborate or just catch up, reach out

Brian Parks
bparks@bigfootcap.com

Rob Spangler
rspangler@bigfootcap.com