AXA VENTURE PARTNERS

White Paper
by Benoit Fosseprez, General Partner
& Sarah Gomey, Analyst

Late-Stage VC: Can Europe Back Its Tech Champions?

New York - London - Paris

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Introduction: A Decade of Tech Financing Challenges in Europe

It has been 10 years since Capital Finance published the article “Late-Stage Venture: The Imperative Adaptation Of The Financing Means”, explaining that the tech financing gap in Europe could only be filled by the emergence of a strong ecosystem of European late-stage VC Funds. And yet, as recently as June 2023, Philippe Tibi interviewed by the Financial Times defined the “problem of the missing zero”, i.e., “in Europe, there is a gradual understanding that the order of magnitude for everything is lacking a zero” in the global technology race.

The tech sector has created more value over the last years than any other sector, and this despite the market correction in 2022. Has investors’ positive perception of the technology sector during this period helped Europe to structure a long-awaited late-stage fund ecosystem? What are the reasons? Why do we believe the window of change is now?

Current Landscape: American Dominance in Financing European Tech

We at AVP focus on software-centric tech companies. We love code. So, we checked who has led the financing rounds (over $90m) of software-enabled tech companies since 2018 in Europe. The result is easy to read: American funds. Amongst the 15 most active investors in those rounds, 11 come from the United States, and only one from Europe, Eurazeo. The most active, Softbank, led 19 deals alone, i.e. more than 3 per year, compared to Tiger Global Management with 18 deals. Most tech entrepreneurs in Europe will tell you that these two funds have been disappearing from Europe since the Ukraine war began. Tech stocks have faced a severe valuation correction. Still, the reality remains the same: they have been the top financiers of the more mature tech companies in our continent over the last few years, as the number of deals also massively decreased since Q1 2022. Of course, deal volume does not necessarily mean investment performance, especially for deals signed in 2021 at the peak of valuations in tech. Investors who did not follow the cycle in 2021 were right, but it would be pretentious to say that European Funds have invested less over the last period just because they remained more disciplined on valuation than their American peers. The gap in the number of late-stage deals is too wide to support such an opinion.

Out Of The 10 Most Active Late-Stage VC Investors In Europe, 9 are not European

Top VC Funds Ranked By Number Of Tech Deals Led Or Co-Led In Europe From 2018 To 2023

Rank	Name	HQ - Region	HQ - Country	# of deals led or co-led in Europe
1	SoftBank Investment Advisers	Americas	United States	19
2	Tiger Global Management	Americas	United States	18
3	General Atlantic	Americas	United States	12
4	Tencent Holdings	Asia	China	10
5	Coatue Management	Americas	United States	9
6	Insight Partners	Americas	United States	8
7	TCV	Americas	United States	7
8	General Catalyst	Americas	United States	6
9	Eurazeo	Europe	France	6
10	Teachers' Venture Growth	Americas	Canada	6
11	Accel	Americas	United States	5
12	Sequoia Capital	Americas	United States	5
13	Lightspeed Venture Partners	Americas	United States	5
14	Fidelity Management & Research	Americas	United States	5
15	DST Global	Americas	Cayman Islands	5
16	Qatar Investment Authority	Middle East	Qatar	5
17	Kinnevik	Europe	Sweden	5
18	Bpifrance	Europe	France	4
19	EQT	Europe	Sweden	4
20	Index Ventures	Europe	United Kingdom	4
21	Temasek Holdings	Asia	Singapore	4
22	Permira	Europe	United Kingdom	4
23	Sofina	Europe	Belgium	4
24	Kohlberg Kravis Roberts	Americas	United States	3
25	Novo Holdings	Europe	Denmark	3
26	Goldman Sachs Growth Equity	Americas	United States	3
27	ICONIQ Growth	Americas	United States	3
28	Atomico	Europe	United Kingdom	3
29	Target Global	Europe	United Kingdom	3
30	D1 Capital Partners	Americas	United States	3
31	Lightrock	Europe	United Kingdom	3
32	Dawn Capital	Europe	United Kingdom	3
33	Mubadala Capital	Middle East	United Arab Emirates	3
34	Bond Capital	Americas	Canada	3
35	GIC	Asia	Japan	3

Top European VC Funds Ranked By Number Of Tech Deals Led Or Co-Led In Europe From 2018 To 2023

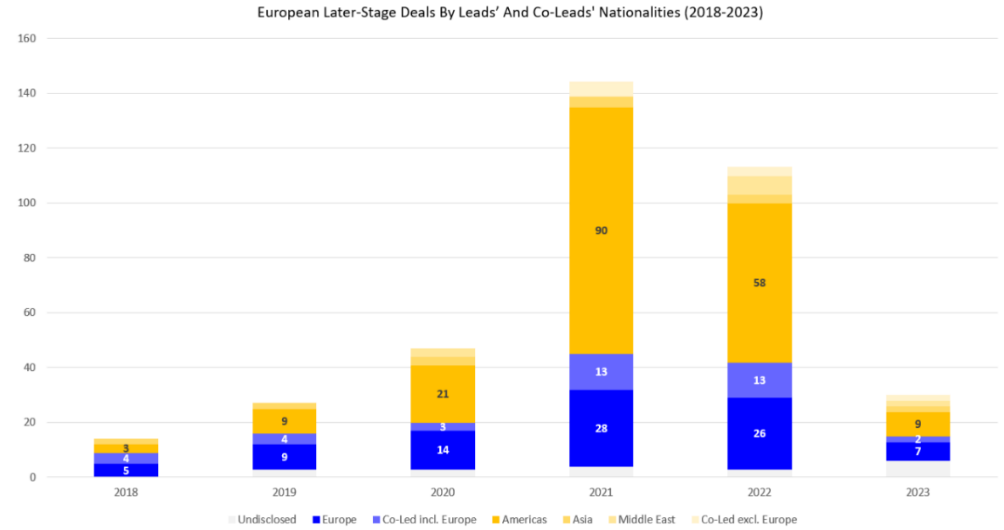
Rank	Name	HQ - Region	HQ - Country	# of deals led or co-led in Europe
1	Eurazeo	Europe	France	6
2	Kinnevik	Europe	Sweden	5
3	Bpifrance	Europe	France	4
4	EQT	Europe	Sweden	4
5	Index Ventures	Europe	United Kingdom	4
6	Permira	Europe	United Kingdom	4
7	Sofina	Europe	Belgium	4
8	Novo Holdings	Europe	Denmark	3
9	Atomico	Europe	United Kingdom	3
10	Target Global	Europe	United Kingdom	3

(1) Source: Pitchbook. Later-stage deals over $90m from Jan-18 to Dec-23. Companies headquartered in Europe in one of the following sectors: HealthTech; Software; FinTech; SOAR; Information Technology; AdTech; AgTech; Artificial Intelligence & Machine Learning; AudioTech; Augmented Reality; B2B Payments; Big Data; Car-Sharing; CleanTech; Climate Tech; CloudTech & DevOps; Construction Technology; Cryptocurrency/Blockchain; Cybersecurity; Digital Health; E-Commerce; EdTech; Ephemeral Content; FemTech; FinTech; FoodTech; Gaming; HealthTech; HR Tech; InsurTech; Legal Tech; Marketing Tech; Mobility Tech; Mortgage Tech; Pet Technology; Real Estate Technology; Restaurant Technology; SaaS; Space Technology; Supply Chain Tech; Virtual Reality

Who in Europe has been active in the same period? Eurazeo, Kinnevik, and BPI France led the game, with respectively 6, 5, and 4 deals led or co-led in the scope analyzed. The top 10 European investors led 40 deals in 6 years, less than the top 3 American investors with 49 deals led. The United Kingdom, with 4 representatives Index, Permira, Atomico, and Target Global is the most represented area in the European top 10, which also says a lot about the Continental European ecosystem of late-stage funds.

Based on such research, we must acknowledge that our European tech champions still depend on the US capacity to fund them. This dependence became clearly visible in 2023, the year when US late-stage funds refocused on their home market. The below analysis demonstrates that Europe is not yet ready to compensate for the disappearance of US late-stage funds from the European tech funding scene.

The European Soaring Tech Ecosystem Attracted Many Foreign Late-Stage VC Funds That Went Back To Their Homelands When The Bubble Exploded



(1) Source: Pitchbook. European later-stage deals over $90m from Jan-18 to Dec-23. See the precedent figure for details on the sectors. 2

Root Causes: Private Equity Dynamics and Tech Sector Evolution

The lack of Late-Stage Funds in Europe has several root causes.

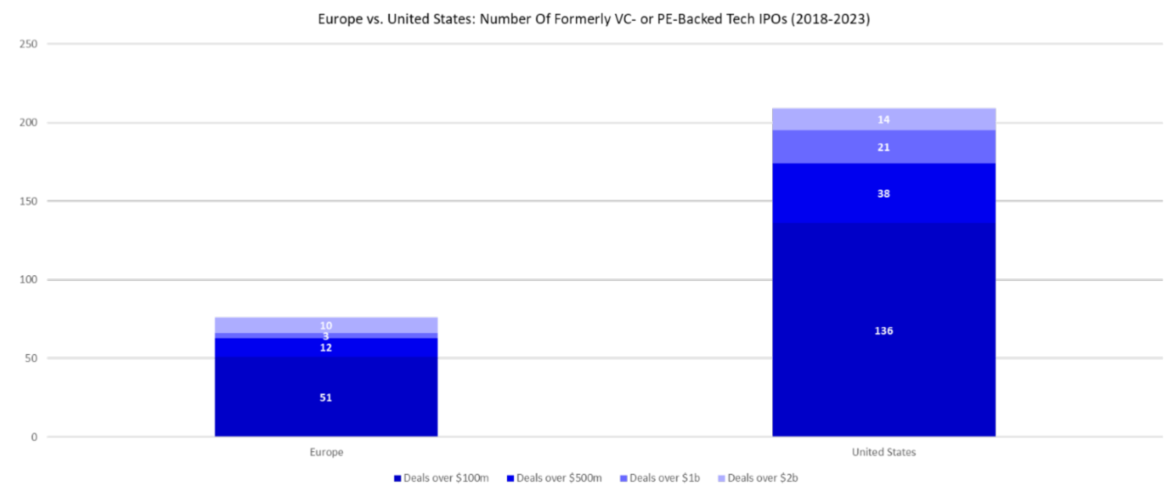
First, if the European private equity sector was well developed even before the GFC, it was underrepresented in Tech/VC funds and overrepresented in LBO funds. The tech sector boom in the 2010s was driven by the accelerated digitalization of B2B flows and generated thousands of start-ups whose funding rules disrupted the traditional market. Banks would never fund EBITDA-negative companies far from reaching profitability, despite massive addressable markets, product market fit, and hypergrowth. As a former banker, I must confess this logic was understandable, only a few years after the trauma of the GFC. Private equity players developed their successful business models on a strict segmentation of companies based on cash-flow generation, capital efficiency improvement potential, and debt leverage. This was not adapted to the new generation of tech companies favoring hypergrowth over profitability in the short term, such hypergrowth allowing them to reach profitability via healthy margin on variable costs, measured by their "unit economics" (i.e., CAC Payback and LTV/CAC ratio). So, while Europe has had an efficient and successful LBO ecosystem, it could not convert it into a successful late-stage VC ecosystem overnight: metrics are different, banks can barely add debt leverage to unprofitable companies, and late-stage investors are usually not in control of companies hence not in a position to decide alone on an exit date. While the LBO sector gave birth to many different asset classes – mezzanine funding, MBO, LBO co-invest, etc., – Late Stage could hardly be a natural continuation of the LBO ecosystem. Mentalities, risk/reward ratios, control requirements, and DPI horizons are just too different.

Of course, many specialized Tech Investment players grew in the 2010s in Europe such as Partech, Balderton, Creandum, and Frst but the lack of experience of European LPs in tech would prevent them from raising €1.5 to €2bn Growth funds in their first generations. Such funds were only raised by massive private equity platforms entering the growth asset class such as Eurazeo or EQT, not by pure tech players coming from the venture capital world.

Secondly, the US economy has outperformed Europe over the last few years and the technology sector has made up a greater share of US GDP, attracting much more capital to the region. As the European Council on Foreign Relations underlines “In 2008 the EU’s economy was somewhat larger than America’s: $16.2tn versus $14.7tn. By 2022, the US economy had grown to $25tn, whereas the EU and the UK together had only reached $19.8tn. America’s economy is now nearly one-third bigger. It is more than 50 percent larger than the EU without the UK.” No surprise that the US attracted most of the bigger private equity checks, those that are needed by multibillion late-stage funds. Moreover, the technology sector has been doubly responsible for this gap: first, it boosted the US economy over the period, and then, through its fast international expansion via digital means, it also imposed US champions in Europe where key players have been Amazon, Salesforce, Google, Meta, Microsoft. A direct consequence is the learning curve of institutional investors in the technology sectors. US institutional investors have had much more exposure to tech over the last 10 years, creating cash-on-cash returns and confidence that Europe has not yet experienced.

Thirdly, it was hard for GPs to invest in companies on pre-money valuations of more than €400m in Europe when regional exit paths were not providing the targeted returns: Tech IPOs have been too scarce in Europe to be a consistent exit scenario for Tech investors. The below analysis compares the number of IPOs of VC-backed Tech companies in Europe and the United States.

IPOs Have Historically Not Been A Sufficient Exit Route For Tech Late-Stage Deals In Europe



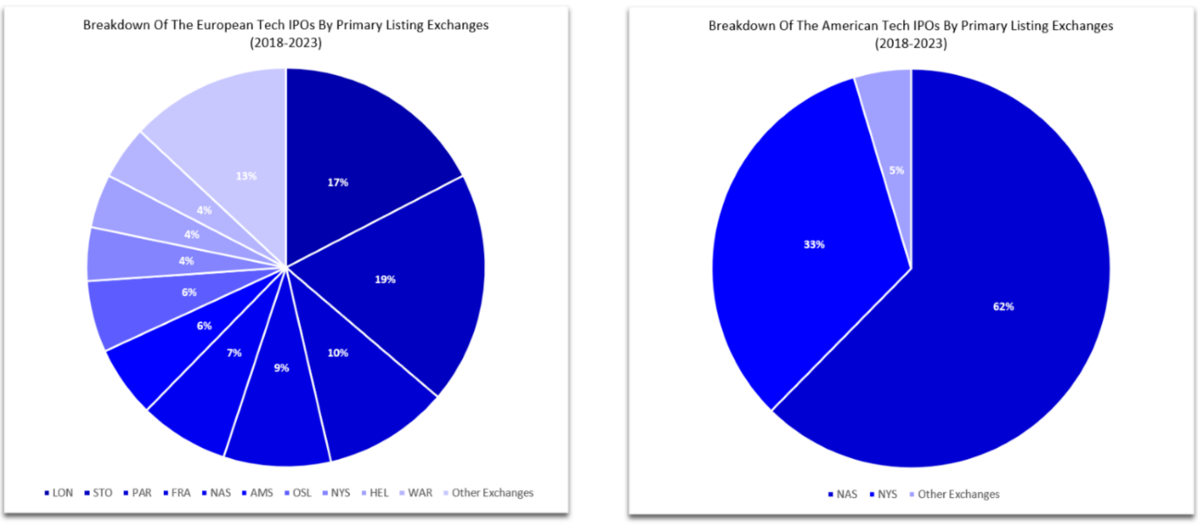
(1) Source: Pitchbook. European and American M&A deals over $500m and IPOs over $100m from Jan-18 to Dec-23. See the precedent figure for details on the sectors.

Comparative Analysis: US vs. Europe in Tech IPOs

There have been about three times more Tech IPOs in the US than in Europe from 2018 to 2023. Focusing on IPOs of companies with a market capitalization over $1bn, there have been 13 in Europe vs. 35 in the US, almost the same ratio. Amongst these 13 European IPOs there was a strong diversity of business models from lithium-battery developer Northvolt to online used-car digital platform Auto1 or end-to-end e-commerce software solution THG. It is hard to find in Europe a pattern of IPOs of pure SaaS models for instance, that would create traction for similar business model entrepreneurs to favor this exit path with confidence.

Another key difference in IPO capacity between Europe and the US is the absence of a common tech-centric listing exchange for European tech candidates, like the Nasdaq in the US. The Nasdaq absorbed 62% of the tech IPOs we analyzed from 2018 to 2023 in the US. This has created a clear, well-identified ecosystem of expertise and talent in the tech IPO industry that attracts IPO candidates from all over the world. Non-Nasdaq IPOs almost exclusively happened on the NYSE with 95% of the US tech IPOs we analyzed listed on either the Nasdaq or the NYSE. This is a huge difference with Europe where the top listing exchange only represented 19% of tech IPOs from 2018 to 2023. It took 5 different exchanges in Europe to reach 62% of the total number of IPOs, i.e., the share of wallet of the Nasdaq alone in the US IPOs in our sample. If we do not have a similar unified technology-centric exchange in Europe, we will struggle to build a powerful tech listing destination on the continent. Nicolas Perard from EIF mentioned to us during an interview that “it is impossible to help all exchanges to develop their tech IPO capacities”, so we need “a political agreement to choose a common European place” to focus on for tech IPOs.

NASDAQ Is The Predominant Listing Exchange For American VC- And PE-Backed Tech IPOs, While European Tech Champions Deal With Disbanded Capabilities

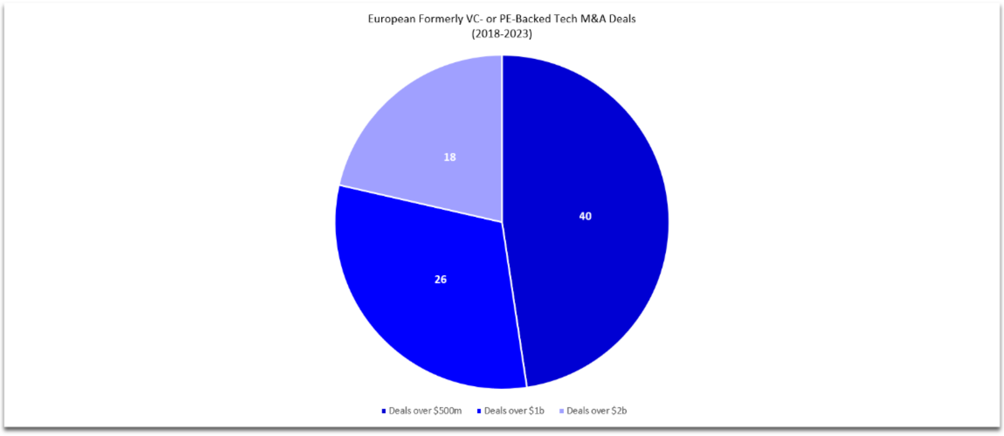


(1) Source: Pitchbook. European and American IPOs over $100m from Jan-18 to Dec-23. See the precedent figure for details on the sectors.

Alternative Exit Paths: M&A and Tech LBOs

In the absence of a sufficient IPO ecosystem for European tech champions, can M&A exits compensate? Certainly, for small to mid-size deals but not yet for late-stage companies. European corporations have not shown an appetite to buy VC-backed companies each year at billion-euro valuations that would correspond to the return expectations of late-stage investors. The recent acquisition of LeanIX by SAP for more than €1.1bn remains an exception in Europe.There have been only 18 acquisitions at more than €2bn valuation of European companies since 2018, i.e., 3 per year. This is not sufficient to provide several European late-stage funds with enough exit scenarios for their late-stage companies in their portfolio.

With Only 18 Deals over $2 Billion in 6 Years, European M&A Deals Do Not Seem To Be Reliable Exits For Late-Stage Investors Yet



(1) Source: Pitchbook. European and American M&A deals over $500m and IPOs over $100m from Jan-18 to Dec-23. See the precedent figure for details on the sectors. 4

Beyond acquisitions by large corporates, Europe can hardly count on Tech LBO funds to offer exit opportunities to late-stage funds. Nicolas Dufourcq, CEO of BPIFrance, exhorted the French and European community at the recent event “Capital Invest” in Paris to develop Tech LBO Funds, in order to offer liquidity to Tech VC funds.

Opportunities Ahead: Unparalleled Window for Tech Investment in Europe

So, is the game over for Europe? No! We at AVP are convinced there is today an unparalleled window of opportunity to promote Tech late-stage investment in Europe, as long as we can structure it properly.

The first success factor is not to limit the investment territory of the fund to Europe. Because exit paths are not yet sufficient in Europe, because the USA has built a unique ecosystem in Tech Late Stage, it is still critical to compete with the best US late-stage Funds to develop investment capacity in North America. This comes with a true local platform and American teams who can bring their local experience and track record and leverage the European capacity of the GP to offer a differentiated value proposal to both American and European late-stage entrepreneurs. Being able to accompany American and European late-stage companies with a true local platform is also a must to win deals with the best European entrepreneurs against US GPs. Of course, the long-term vision of the European Late Stage should not be to send all the best tech European companies to IPO on the Nasdaq. But, to build a learning curve on all exit paths, the future leading tech investment platforms in Europe should be able to offer the best companies any exit path, learn from the best practice of this exchange, and contribute to the development of the tech IPO pipeline in Europe leveraging this experience.

The second success factor is the ability to raise funds large enough to credibly lead €200m to €300m financing rounds, i.e., €1.5bn or more. We analyzed earlier that the total number of European Funds with a size beyond €1.5bn is too limited to propose a true alternative to American funds. In that domain, European governments have taken decisive initiatives to support the launch of such billion-euro funds. The EIF's European Champions Tech Initiative launched in February 2023 with EIB resources and contributions from France, Germany, Spain, Italy, and Belgium consists of a fund of funds with "€3.75bn of capital to tackle the European scale-up gap" as explained on the EIF's website. It aims to make 10 to 15 investments in large tech funds of €1bn or more that will support "promising high-tech companies (…) to compete on a global scale whilst staying in Europe". This initiative also creates awareness about Europe through large institutional investors from other continents, which is critical. Nicolas Perard from EIF underlined that in the 2023 geopolitical context, Europe is perceived as a place of political stability by the biggest institutional investors from other continents. In France, the second "Tibi Initiative" that aims at directing more institutional money into French tech funds now includes Late-Stage Funds. With a total envelope of €7bn from 2023 to 2026, this initiative will naturally drive more French institutional allocations into Late-Stage Tech funds, beyond the support that the French Banque Publique d'Investissement has been providing to French GPs for several years now. This mix of government money and institutional money going into tech funds will help secure enough European late-stage Funds to accompany the evolution of the European tech investment ecosystem toward regional pre-IPO rounds and then, eventually, toward European tech IPOs.

We are convinced there has never been a better window to accelerate late-stage tech investment in Europe: institutions have implemented dedicated programs to support fundraising, valuations came back to areas of normality after the 2021 cycle peak, despite the market correction in 2022 technology has been a rewarding area of investment for institutional investors over the last decade, Europe now counts several tech champions ready to compete with global leaders in their industries, and finally, Europe is the most dynamic place in the world in the fight against climate change which attracts many talented tech entrepreneurs. Let's see in 10 years then!

We invest in great entrepreneurs.

We support outstanding companies.

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