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Executive summary

European Venture Debt

Venture debt – geographic significance

- Venture debt, a solution for fast growing companies that lack the assets or cash flow for traditional debt financing instruments, has existed in the US for over 3 decades and was imported to Europe around 20 years ago.
- As a result of the scale of the VC funding and prevalence of non-bank funding in America, venture debt is more commonplace in the US. It has not gained the same level of traction in Europe, and is still considered niche with just a limited number of players operating in this space in Europe.
- Similarly to its complimentary product, venture capital, majority of European venture debt transactions are concentrated around UK, France and Germany. In order to increase the venture debt prevalence in other jurisdictions, efforts should be made to increase venture capital availability and uptake in the first instance.
- Despite the limited market awareness, venture debt has several benefits that make it a useful tool to support early stage innovative ventures.

About the market

- Market players can be divided into funds, commercial banks as well as national and international promotional banks, each with specific investment criteria and product characteristics.
- The main industries benefitting from this capital are technology and healthcare businesses with the receiving companies characterised by high revenue growth, innovative products and which have often not achieved profitability yet.
- This report explains the main features of venture debt, analyses the venture debt market in Europe in terms of lender universe and jurisdictional differences and compares it to the VC market.
- For the purpose of this study, the traditional venture debt and the venture growth loans have been analysed together and jointly referred to as “venture debt.”
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3. Venture capital landscape in Europe

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1. Introduction to venture debt
Venture debt – key facts

Venture debt is a financing option for fast growing companies looking for additional funding whilst minimising dilution.

What is venture debt?

- Venture debt is a solution for companies (usually venture-backed, but not always) that lack the assets or cash flow for traditional debt financing instruments.
- It is often raised immediately following an equity round, when marketing and diligence reports are readily available.
- Venture debt is typically provided by dedicated venture or growth debt funds and/or banks to rapidly growing companies.
- Venture debt amount is usually equal to c.20-35% of the venture capital raise.
- It provides businesses with a source of funding next to equity, enabling additional funding with less dilution and fewer governance requirements (no board seat and/or voting rights).
- There are two main venture debt option: traditional venture debt (bridge financing, short term) and growth venture debt (growth oriented, long term).

Next to venture capital, we distinguish two types of venture debt: “Traditional” and “Growth”

<table>
<thead>
<tr>
<th></th>
<th>Venture Capital (Equity)</th>
<th>Traditional Venture Debt</th>
<th>Growth Venture Debt</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Business characteristics</strong></td>
<td>Seed to pre-IPO</td>
<td>Medium to late venture capital stage, high growth</td>
<td>Late venture capital/growth stage</td>
</tr>
<tr>
<td><strong>Ticket size</strong></td>
<td>Depends on stage of development</td>
<td>€0.5m - 20m (€2-3m on average)</td>
<td>€5m – 50m</td>
</tr>
<tr>
<td><strong>Dilution</strong></td>
<td>Yes, 10 to 50%, will also receive a board seat</td>
<td>Generally a small fraction of equity &lt;1%, due to warrant</td>
<td>Generally none</td>
</tr>
<tr>
<td><strong>Covenants</strong></td>
<td>N/A</td>
<td>No financial covenants, but other restrictions may apply</td>
<td>1-2 covenants, P&amp;L and/or balance sheet tests</td>
</tr>
<tr>
<td><strong>Tenor</strong></td>
<td>Usually 5-8 followed by sale or IPO</td>
<td>1-4 years</td>
<td>3-5 years</td>
</tr>
<tr>
<td><strong>Time to raise funds</strong></td>
<td>6-12 months</td>
<td>2-4 months</td>
<td>2-4 months</td>
</tr>
<tr>
<td><strong>Repayment strategy</strong></td>
<td>IPO / trade sale</td>
<td>Equity funding round</td>
<td>Repayment from operating cash flows</td>
</tr>
</tbody>
</table>

Flexibility vs. dilution

- Traditional Venture Debt: high flexibility, medium dilution.
- Growth Venture Debt: high flexibility, low dilution.

Venture Capital (Equity)
Funding options for companies at various stages of growth

Overview of various funding options throughout the company life cycle for innovative businesses

<table>
<thead>
<tr>
<th>Company stage</th>
<th>Founding stage</th>
<th>Acceleration stage</th>
<th>Maturity stage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial parameters</td>
<td>Start-up phase – Series B+</td>
<td>Ramp-up phase</td>
<td>Rapid acceleration</td>
</tr>
<tr>
<td>Equity &amp; Venture capital</td>
<td>EBITDA</td>
<td>EBITDA</td>
<td>EBITDA</td>
</tr>
<tr>
<td>Venture debt</td>
<td>Operating cash flow</td>
<td>Operating cash flow</td>
<td>Operating cash flow</td>
</tr>
<tr>
<td>Growth capital</td>
<td>Free cash flow</td>
<td>Free cash flow</td>
<td>Free cash flow</td>
</tr>
<tr>
<td>Asset based lending</td>
<td></td>
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<tr>
<td>Mezzanine</td>
<td>TLB / Unitranche</td>
<td></td>
<td>Senior debt</td>
</tr>
</tbody>
</table>

* Key: 🔴 Negative, 🔵 Break even, 🟢 Positive
When to use traditional venture debt

Venture debt can be attractive for companies that seek additional funds to accelerate growth without raising additional equity

<table>
<thead>
<tr>
<th>The value of venture debt</th>
</tr>
</thead>
<tbody>
<tr>
<td>Venture debt can be attractive in a number of ways:</td>
</tr>
</tbody>
</table>

1. **Increase runway to next milestone**
Venture debt can extend the cash runway of a company to the next valuation driver. The valuation is typically based on achieving milestones. As such, the optimal time to raise funds is immediately following the completion of a milestone. Venture debt has the potential to increase the runway of companies and increase the probability of achieving the next milestone / valuation driver resulting in a higher valuation at the next equity round thereby substantially reducing dilution.

2. **Extend runway to cash flow positive**
Venture debt can extend the cash runway of a company to become cash flow positive. Instead of raising a large equity round, a company could raise a smaller amount of equity and then leverage venture debt to fund the company until it receives its first revenue from customers, ensuring Series C is raised at a much higher valuation or completely eliminate the last round of equity financing thereby substantially reducing dilution.

3. **Provide “insurance” for delays**
Venture debt can serve as a cushion in the case of potential delays. In the event of a cash shortage a company may consider to launch an additional equity round. However, this will most likely be a highly dilutive financing round whereas venture debt could have helped bridge this gap until the company is back on track (i.e. achieves a more favourable valuation and lower dilution).

Source: Trinity Capital Investments website and Deloitte analysis

* Figures are for illustrative purposes only
Key considerations when deciding for venture debt

Venture debt lenders typically look at a number of predetermined characteristics to assess the borrower attractiveness.

### Key determinants of obtaining a loan

<table>
<thead>
<tr>
<th>Revenue model</th>
<th>Credit risk</th>
<th>Collateral</th>
<th>Profitability</th>
<th>Use of proceeds</th>
<th>Sponsor backed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-recurring</td>
<td>Subscription / recurring</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Concentrated / high churn</td>
<td>Diverse / sticky</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&lt; €5M revenue</td>
<td>&gt; €20M revenue</td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Limited</td>
<td>Substantial</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Outside 2 years</td>
<td>Recently achieved</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Liquidity</td>
<td>Growth</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Founder / angel group</td>
<td>Reputable VC / PE</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Spinta Capital website and Deloitte analysis
Key benefits of venture debt

Supporting business growth

Additional capital to fund growth
- Provides additional capital in between VC rounds for a number of projects:
  - Roll-out of new sites
  - Extending business cash runway
  - Providing working capital
  - Increasing staff numbers
  - Marketing and sales expansion
  - Product development
  - M&A activity

Flexible structure
- Adjusted to business needs
- Quicker process than VC fundraising and requires less management distraction

Avoiding dilution
- Maintaining control over equity (minimal dilution as a result from warrants)
- Debt investors don’t have a board seat or voting rights

Cheaper than equity
- Debt financing is cheaper than equity
- Assuming strong growth of the company, adding leverage will increase the percentage returns for the founders and VC investors
- Tax deductible interest payments

No need to price next round at an unfavorable valuation
- Using venture debt, it is possible to avoid excessive dilution as a result of temporarily suppressed valuation

“Insurance” against cash shortage
- The additional funding acts as an “insurance policy” against liquidity shortage in case of any delays to the business plan
Key downsides of venture debt

Increased probability of default is the key downside

Cash drain for the business
• Repayments during the first stages of a venture’s life-cycle can negatively impact the company’s financial health (especially in case of short-term bridge loans)

Possible default
• Inability to repay principal and interests can lead to default

Possible dilution
• Venture debt can create dilution upon default if the debt-holders exercise their option to convert debt into equity

Pledge on intellectual property
• In case of liquidation, the venture debt lender typically requires the right to the patents

Covenants
• Restrictive covenants can limit management’s freedom to pursue a business strategy coherent with the company’s vision

Lack of third-party valuation
• The business does not receive an official valuation ascertaining its growth
### Types of venture debt providers

Funds, banks and IFIs are the main providers of venture debt

<table>
<thead>
<tr>
<th>Venture debt providers comparison</th>
<th>Funds</th>
<th>Banks</th>
<th>International financial institutions (IFIs)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Relationship duration</strong></td>
<td>• Usually 2-5 years of investment</td>
<td>• Long term view, future corporate client pipeline</td>
<td>• Long term view</td>
</tr>
<tr>
<td><strong>Pricing</strong></td>
<td>• Typically more expensive, dictated by hurdle rates agreed with LPs of the fund</td>
<td>• Typically cheaper, balance sheet funding</td>
<td>• Typically cheaper, balance sheet funding</td>
</tr>
<tr>
<td><strong>Ancillary business required</strong></td>
<td>• No</td>
<td>• Yes (e.g. deposits, credit cards, FX)</td>
<td>• No</td>
</tr>
</tbody>
</table>
| **Warrants**                     | • Typical for early stage venture debt  
• Higher probability to be exercised | • Typical for early-stage venture debt  
• Higher probability to be sold back | • Usually not applicable |
| **Business characteristics**     | • High growth businesses | • High growth businesses | • Innovative, socially beneficial and responsible businesses |
| **Geographic focus**             | • Demand and profit driven | • Demand and profit driven | • Social objectives of equal access to capital to boost the economy |
| **Examples**                     | • Boost & Co.  
• Bootstrap Europe  
• Harbert European Growth Capital  
• Kreos Capital | • Barclays  
• Goldman Sachs  
• Silicon Valley Bank | • European Investment Bank  
• KFW Bank |

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## Overview

### Venture debt product comparison

<table>
<thead>
<tr>
<th>Category</th>
<th>Traditional venture debt</th>
<th>Growth loan</th>
<th>EIB Venture Debt</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Business characteristics</strong></td>
<td>• Medium to late venture capital stage experiencing high growth</td>
<td>• Late venture capital/growth stage</td>
<td>• Late venture capital/growth stage</td>
</tr>
<tr>
<td><strong>Ticket size</strong></td>
<td>• €0.5m - €20m</td>
<td>• €5m – €50m</td>
<td>• €7.5m – €50m</td>
</tr>
<tr>
<td><strong>Tenor</strong></td>
<td>• 1 - 4 years</td>
<td>• 3 - 5 years</td>
<td>• 5 - 7 years</td>
</tr>
<tr>
<td><strong>Interest rate (excl. warrants)</strong></td>
<td>• 9% - 15%</td>
<td>• 6% - 12%</td>
<td>• 3% - 10%</td>
</tr>
<tr>
<td><strong>Dilution</strong></td>
<td>• Generally a small fraction of equity &lt;1.5%, due to warrant</td>
<td>• May include a small fraction of equity &lt;1%, due to warrant</td>
<td>• Generally a small fraction of equity due to warrant, exercised in cash</td>
</tr>
<tr>
<td><strong>Financial covenants</strong></td>
<td>• None</td>
<td>• 1-2 covenants, P&amp;L and/or balance sheet tests</td>
<td>• None</td>
</tr>
<tr>
<td><strong>Industry focus</strong></td>
<td>• Primarily technology and healthcare, but include also other sectors • Focuses on future profitability</td>
<td>• Primarily technology and healthcare, but include also other sectors • Focuses on future profitability</td>
<td>• R&amp;D-driven industries • Includes biotechnology, software, renewable energy, etc.</td>
</tr>
</tbody>
</table>

Source: Venture debt providers’ websites and market research conducted by Deloitte

Source: EIB
EIB Venture Debt

Overview

Why is EIB financing attractive?

- The EIB offers **longer maturities at attractive pricing** (compared to alternative sources of finance)
- **Highly flexible growth capital** without dilution of shareholders
- The reputation of the EIB can provide a **quality stamp** and **positive signalling effect** for the company
- EIB does **not offer other banking services**, such as FX, swaps, etc.
- Advantageous source of funding besides primary bank facilities
- The EIB pursues a **long-term lending strategy** and does not sell its exposure to third parties

Overview

- The EIB partners with the European Commission to support growth and investments in Research & Innovation (**“R&I”**)
- The EIB provides long-term financing solutions to public and private companies
- The company should have significant innovation potential and / or be a Research & Innovation driven enterprise
- The company is a fast-growing enterprise, as measured by:
  - Employment
  - Turnover
  - Factors related to R&I

Sector focus

- Software and Tech
- Life Science
- Biotech & Pharma
- Clean-tech and Renewables
- Engineering and Automation

Geographic presence

© 2019 Deloitte Tax & Consulting  Source: EIB
2. Venture debt landscape in Europe
Geographic differences between the US and Europe

Usage of venture debt differs significantly between both regions

Overview

Venture debt has existed in the US for over 3 decades and appeared in Europe around 20 years ago. Despite a number of years on European soil, the product has not achieved the same level of success as in the US, both in terms of the absolute numbers as well as in comparison to venture capital. The potential reasons for these geographic differences fall into two main categories:

1) Why is the European VC market smaller
   • Lack of fully developed start up ecosystem (no Nasdaq equivalent, high geographic fragmentation of financial markets)
   • A survey* of VC investors in both regions shows that the European VCs hold their investments for a longer period of time (3.6 years in Europe vs 2.9 years in America) and replace management less frequently (19% vs. 34%) which indicates that they might be more risk averse and reluctant to make a tough decision to cut losses early
   • The same survey shows that European VCs invest in their own region more frequently (60 percent vs. 46 percent) thus limiting a more even expansion across Europe

2) Why is venture debt less popular among European VC investors
   • European companies are used to traditional bank financing and may not be familiar with alternative sources of debt funding
   • VC investors and entrepreneurs are more risk averse thus do not want to leverage the company even if it would increase the growth trajectory

Deal distribution across Europe is broadly in line, with the exception of the UK.

- Western EU (excl. UK): Venture Capital: 50%, Venture Debt: 41%
- UK: Venture Capital: 15%, Venture Debt: 35%
- Northern EU: Venture Capital: 12%, Venture Debt: 15%
- Southern EU: Venture Capital: 16%, Venture Debt: 5%
- Central EU: Venture Capital: 2%, Venture Debt: 2%
- Eastern EU: Venture Capital: 3%, Venture Debt: 1%

Out of the total sample of 285 European venture debt deals published on the lenders’ websites*:
- 41% companies were based in Western EU
- 35% in the UK
- 15% in Northern EU
- 5% in Southern EU
- 2% in Central EU
- 1% in Eastern EU

Proportion of venture debt funding in Western Europe is in line with the venture capital funding to these jurisdictions.

UK is disproportionately represented in venture debt funding compared to venture capital funding, at the expense of Southern Europe (see slide 26).

*Providers considered are: EIB, Bootstrap Europe, Boost & Co., Columbia Lake Partners, Harbert European Growth Capital, IPF Partners, Kreos Capital.
## European venture debt – providers by geographic focus

Venture debt players are mostly focused on UK and Western Europe; Nordics and Central Europe follow in terms of investments.

### Selected venture debt players by geographic focus

<table>
<thead>
<tr>
<th>Providers / Regions</th>
<th>Western Europe</th>
<th>UK</th>
<th>Central Europe</th>
<th>Eastern Europe</th>
<th>Northern Europe</th>
<th>Southern Europe</th>
</tr>
</thead>
<tbody>
<tr>
<td>Barclays</td>
<td></td>
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<td></td>
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</tr>
<tr>
<td>Boost&amp;Co.</td>
<td></td>
<td>✓</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Bootstrap Europe</td>
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<td>✓</td>
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<td>Columbia Lake Partners</td>
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<td>✓</td>
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<td>✓</td>
</tr>
<tr>
<td>Harbert European Growth Capital</td>
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<td>✓</td>
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<td>✓</td>
<td>✓</td>
<td>✓</td>
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<tr>
<td>IPF Partners</td>
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<td></td>
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<tr>
<td>Kreos Capital</td>
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<td>✓</td>
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<tr>
<td>Silicon Valley Bank (SVB)</td>
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<tr>
<td>TPG</td>
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<td>✓</td>
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<td>✓</td>
</tr>
</tbody>
</table>

Source: Venture debt providers’ websites and other public sources

Western Europe: Belgium, France, Germany, Ireland, Luxembourg, Netherlands
Eastern Europe: Bulgaria, Croatia, Estonia, Hungary, Latvia, Lithuania, Romania, Slovenia
Northern Europe: Sweden, Finland, Denmark
Southern Europe: Italy, Spain, Portugal, Greece, Malta, Republic of Cyprus
Central Europe: Austria, Czech Republic, Poland, Slovakia
## European venture debt – providers by sector focus

Venture debt players are mostly focused on IT and software companies, followed by healthcare and clean tech ventures.

<table>
<thead>
<tr>
<th>Providers / Sectors</th>
<th>IT (excl. Software)</th>
<th>Software</th>
<th>Healthcare</th>
<th>Pharma</th>
<th>Biotech</th>
<th>Clean tech</th>
<th>Engineering</th>
<th>Others</th>
</tr>
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<tbody>
<tr>
<td>Barclays</td>
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<td>Global Growth Capital</td>
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<td>✓</td>
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</tr>
</tbody>
</table>

Source: Venture debt providers’ websites and other public sources
European venture debt – amounts invested to date

The estimated amount of venture debt invested in European companies by a sample of selected providers is over €5 bn

<table>
<thead>
<tr>
<th>Provider</th>
<th>Amount invested to date (€m)</th>
<th>Number of deals</th>
<th>Years of activity in venture debt</th>
<th>Total capital invested to date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kreos</td>
<td>2,300</td>
<td>80</td>
<td>20</td>
<td></td>
</tr>
<tr>
<td>EIB</td>
<td>1,800</td>
<td>200</td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>Harbert European Capital</td>
<td>400</td>
<td>221</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bootstrap</td>
<td>332</td>
<td>98</td>
<td>17</td>
<td></td>
</tr>
<tr>
<td>Barclays</td>
<td>211*</td>
<td></td>
<td>5</td>
<td></td>
</tr>
</tbody>
</table>

* Amount translated from GBP using GBP/EUR FX rate of 1.17, as of 15 Mar 2019
Source: Venture debt providers’ websites and market research conducted by Deloitte
European venture debt – fundraising

Fundraising by venture debt providers

Fundraising amount by selected venture debt providers (€m)

Key: 100

Barclays 117*
Barclays 117*
Global Growth Capital

IPF 105
Harbert 115
Kreos 400

Barclays
Bootstrap 100
Harbert 215
Kreos 700


* Amount translated from GBP using GBP/EUR FX rate of 1.17, as of 15 Mar 2019
Source: Venture debt providers’ websites and market research conducted by Deloitte
3. Venture capital landscape in Europe
European venture capital – capital raised by funding stage

Capital raising activity nearly doubled in the last 5 years, reaching €7.7bn in 2017

**Description**
- The total amount of funds raised almost doubled over the last 5 years, going from €3.9bn in 2012 to €7.7bn in 2017
  - Early stage capital raising increased from €1.7 to €2bn
  - Late stage venture capital raising significantly increased over the period, but its percentage out of the total shrank
  - Venture stage raising, which includes both strategies within the same fund, almost tripled, going from €1.9bn in 2012 to €5.2bn in 2018
  - Overall, there has been a shift to funding generalist VC companies

**Source:** Invest Europe

**Description**
- Whilst the amounts raised almost doubled, the number of VC funds only increased by 12% from 146 to 163 during the same period
  - The total number of funds in 2012 was 146, mainly focused on venture stage and early-stage
  - A lower percentage of funds was focused on later stage (c. 6%)
  - At the end of 2017, the distribution in terms of funding stage has not changed significantly
  - Compared to the amounts raised as per the graphs above, the bulk of new investments went to the established generalist VC companies

**Source:** Invest Europe
European venture capital – breakdown by sector

Capital invested in European ventures doubled over the last 5 years, reaching €6.4bn in 2017 with the IT sector attracting 45% of total investments.

The total amount of funds invested in European ventures doubled over the last 5 years, going from €3.2bn in 2012 to €6.4bn in 2017.

The sectors that historically attracted most capital were Information Technology and Biotech / Healthcare:
- Funds invested in IT spiked from €1.2bn in 2012 to €2.9bn in 2017, with an increased share of investment from 36% to 45%.
- Investments in Biotech and Healthcare rose as well, from €899m in 2012 to €1.5bn in 2017 although the share of investment dropped from 28% to 23%.
- Investments in the energy sector dropped from €334m (10%) in 2012 to €265m (4%) in 2017.
- Investments in the financial and insurance activities surged from €74m (2%) in 2012 to €437m (7%) in 2017.

Source: Invest Europe
UK, France and Germany have attracted nearly 65% of the €6.4bn European venture capital amount invested in 2017.

The total venture capital raised by European companies in 2017 amounts to €6,435m.

UK, France and Germany attracted 65% (€4,168m) of the total capital invested in European ventures.

Spain, Netherlands, Sweden and Switzerland follow, accounting for 22% (€1,362m).

Source: Invest Europe
3,756 companies were financed through venture capital in 2017, with an average ticket size of €1.7m

**Number of ventures financed in 2017**

- **France** and **Germany** lead the way, with 724 and 651 companies financed, respectively.
- **UK** had the 3rd place, with 539 companies financed; but it showed the highest ticket size in the top 15 EU countries.

**Top 15**

<table>
<thead>
<tr>
<th>Country</th>
<th>Avg. ticket size (€k)</th>
</tr>
</thead>
<tbody>
<tr>
<td>United Kingdom</td>
<td>3,278</td>
</tr>
<tr>
<td>France</td>
<td>1,742</td>
</tr>
<tr>
<td>Germany</td>
<td>1,750</td>
</tr>
<tr>
<td>Spain</td>
<td>1,098</td>
</tr>
<tr>
<td>Netherlands</td>
<td>1,374</td>
</tr>
<tr>
<td>Sweden</td>
<td>1,072</td>
</tr>
<tr>
<td>Switzerland</td>
<td>1,948</td>
</tr>
<tr>
<td>Belgium</td>
<td>1,636</td>
</tr>
<tr>
<td>Finland</td>
<td>1,048</td>
</tr>
<tr>
<td>Ireland</td>
<td>2,099</td>
</tr>
<tr>
<td>Austria</td>
<td>2,183</td>
</tr>
<tr>
<td>Italy</td>
<td>1,208</td>
</tr>
<tr>
<td>Denmark</td>
<td>1,748</td>
</tr>
<tr>
<td>Norway</td>
<td>884</td>
</tr>
<tr>
<td>Poland</td>
<td>1,760</td>
</tr>
</tbody>
</table>

**Top 15 average** | **1,655**

Source: Invest Europe

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4. Appendix
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