INDUSTRY VENTURES

THINNING THE HERD: ~50% OF UNICORNS SHOULD NO LONGER BE UNICORNS – A VC SPECIALIST'S VIEWPOINT

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With 700+ fund investments and 400+ company investments in venture to date, many of our LPs, GPs, and founders ask about what is happening to "Unicorns"[1] valuations. And specifically, what is happening to the so-called herd of "ZIRPicorns" that attained Unicorn status in the heady market of 2021/2022?[i] How many companies have lost their magical horn, i.e., are now "Horses"?[ii] And, at the very least, we've employed enough mythical terminology and analysis to entertain you.

We have proprietary data on 391 Unicorns via our direct or indirect exposure (i.e., fund investments), or approximately one-third of the companies on CB Insights Unicorn list.[iii] Through these investment, we have access to information on revenue, growth rates, and valuations. In order to determine Unicorn status, we evaluated: (1) accounting values of the companies in audited financial statements, (2) where bid/ask and clearing prices were for secondary market trades, (3) subsequent funding rounds, i.e., whether a company has raised capital since the peak valuations of 2021 and early 2022, and (4) underlying revenue, EBITDA and growth rates of these companies.

OBSERVATION #1: OVER ONE-FOURTH OF ALL ACTIVE UNICORNS HAVE ALREADY BEEN DE-HORNED BY EITHER FMV MARKS OR SECONDARY VALUATIONS

We utilized two valuation methodologies to evaluate our list of Unicorns; each methodology had differing dataset coverage. The first valuation methodology employed was fund fair market value (FMV) marks or new rounds (which funds typically mark to once they occur and typically hold for at least 12 months) with over 50% coverage of our dataset. The second methodology employed was secondary valuations (where companies are trading in the market) with 33% coverage of our dataset. The lower coverage in secondary valuations is due to many of these companies having limited data points to draw accurate pricing from or no presence at all in the secondary marketplace.

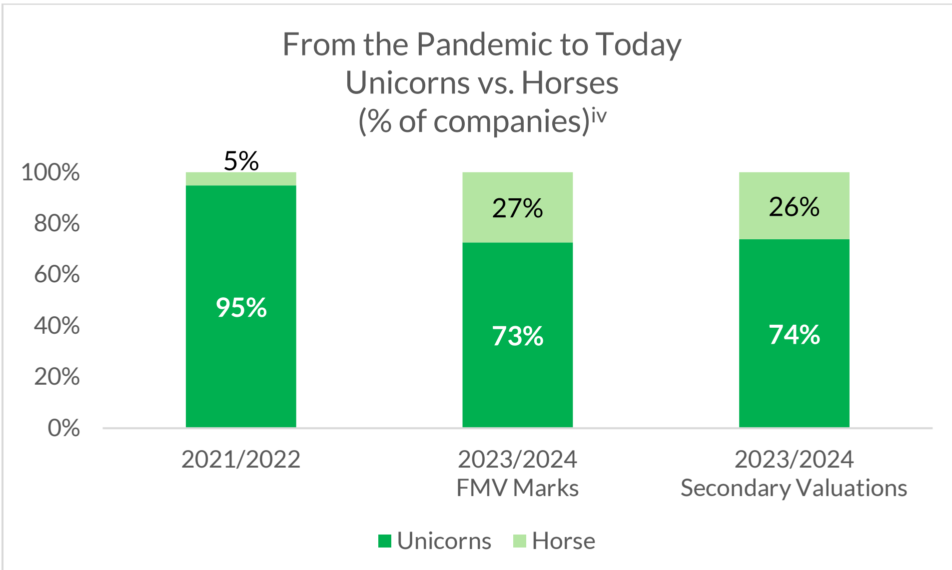
The list of Unicorns dehorned through our two methodologies has limited overlap. Of the total list of Horses we identified through both methodologies, only a few companies were less than $1B in valuation and had both fund valuations and secondary exchange pricing.

Over 80% of all Unicorns (companies that were valued at $1B+ at any point) with FMV data in our sample dataset are sitting at lower valuations than they were after the tech reset following 2021/2022. Not only are they falling in valuation, but nearly 30% have fallen to Horse status by 2023/2024, meaning they are now valued at under $1B by FMV marks or new rounds.

[1] Companies valued at $1B+ in funding rounds

Comparatively, only 5% of the Unicorn list minted prior to 2021/2022 was a Horse by this same methodology in the 2021/2022 time period.[iv]

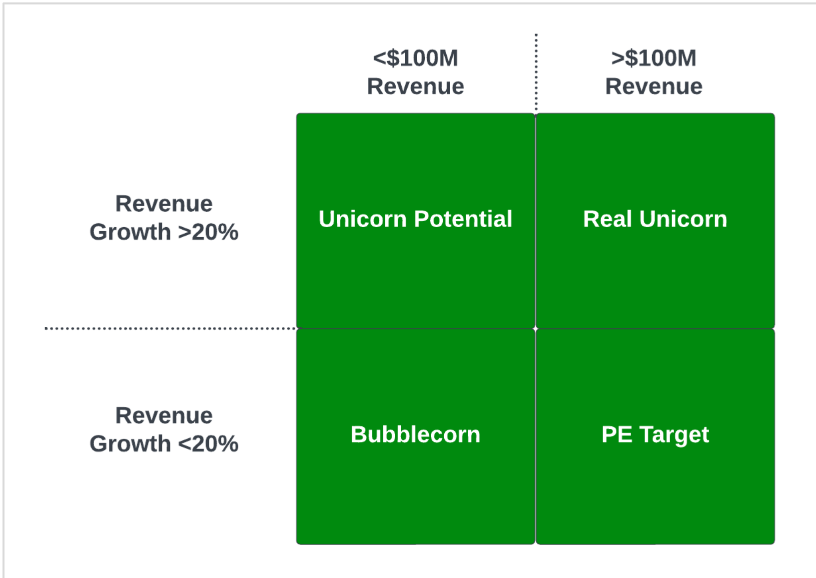
Interestingly, the result is almost identical when using secondary valuations for the Unicorns. The number of "Unicorns" that should be labeled as Horses is nearly 30% again. Now, we could attribute this to managers valuing their investments in line with the secondary market pricing, but many of the Unicorns we reviewed have no visible presence on the secondary market and/or have minimal closed transactions; in these cases, secondary market pricing would not inform fund valuations.



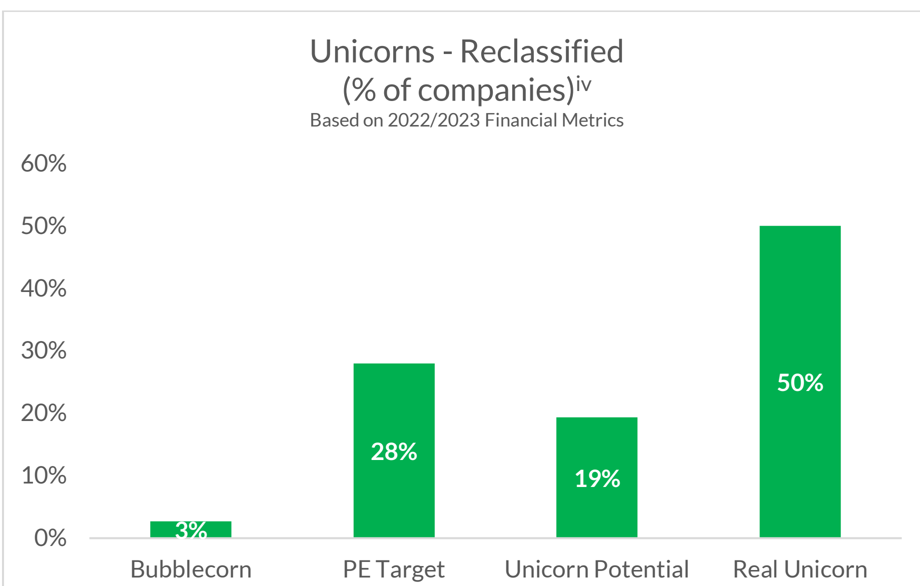
The valuation comparison in FMV marks and secondary valuations underscores the overall market suppression of company valuations even among the still-Unicorn population. During 2021 and 2022 we were in unforeseen territories with Unicorns as we had more crowned in that time period than any other. However, this has resulted in many companies fictitiously reaching such status flying on this bubble's wings and not having the true merits of the original pre-2021 Unicorns. But is this all the fault of the companies themselves or were more macroeconomic factors at play in this rising Horse population?

We believe much of this can be attributed to the high multiples that companies were valued at during 2021/2022, which was reflective of the overall public markets, and a good portion of the write-downs we see today can also be attributed to the performance of the public comps.[v] In addition to the public valuation compression, many of the Horses have significantly missed the plans they raised their Unicorn rounds on, whether that is due to macro headwinds or idiosyncratic issues.

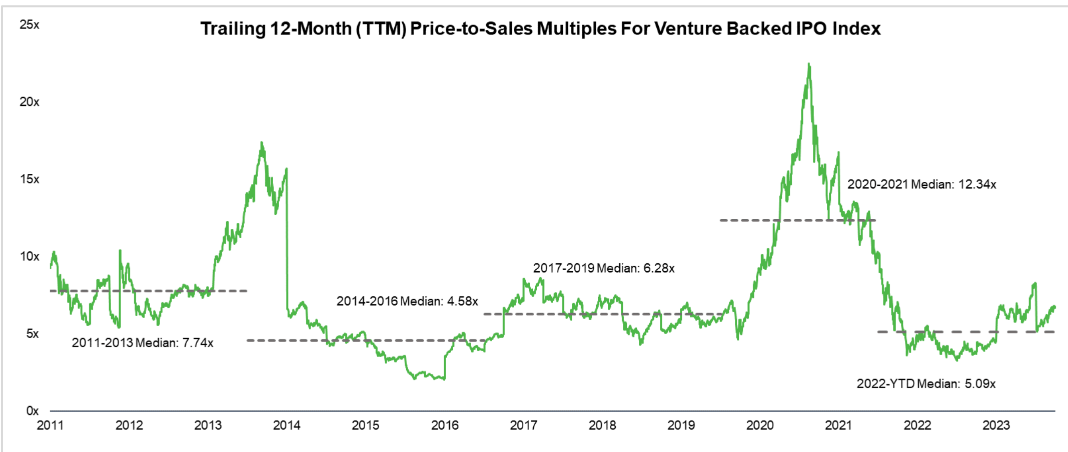
OBSERVATION #2: MANY UNICORNS ARE NOW "PE TARGETS" BASED ON REVENUE AND GROWTH METRICS



Revenue scale and growth are perhaps the best indicators of private growth company value. We looked at the 391 companies and defined them as "Scaled" if they have $100M of revenue or greater. To categorize companies, we also used 20% growth as a threshold, as the median NTM growth rate of the SaaS businesses that comprise the Bessemer Cloud Index is 19%.[vi] All "Bubblecorns" and many of the companies falling into the "PE Targets" or "Unicorn Potential" category could be categorized as a Horse based on valuation. Still, we decided to break them down further on revenue scale and growth.[iv]



What we found is that we believe 50% of companies in our data set to still be worthy of Unicorn designation using the scale/growth criteria above. We believe 3% of the names are no longer Unicorns and have the hallmarks of companies that would raise at a <$1B valuation if they went to market for a new fundraising round today; these are the aforementioned "Bubblecorns." Many of these companies, however, raised meaningful-sized rounds (often the rounds that designated them a Unicorn) and have not had to raise or seen a public repricing. Within our portfolio, we have seen a number of these names decrease their growth rates from >40% to <20% to bring down cash burn and are trying to find a way to reaccelerate with the capital they have on hand. While these companies may not be "Bubblecorns" forever, absent an acceleration in growth or a significant increase in scale, we think these companies will either see a market repricing and officially become Horses again (either in an exit or a fundraise) or continue to linger in venture portfolios and likely be written down by the GPs holding them over time.

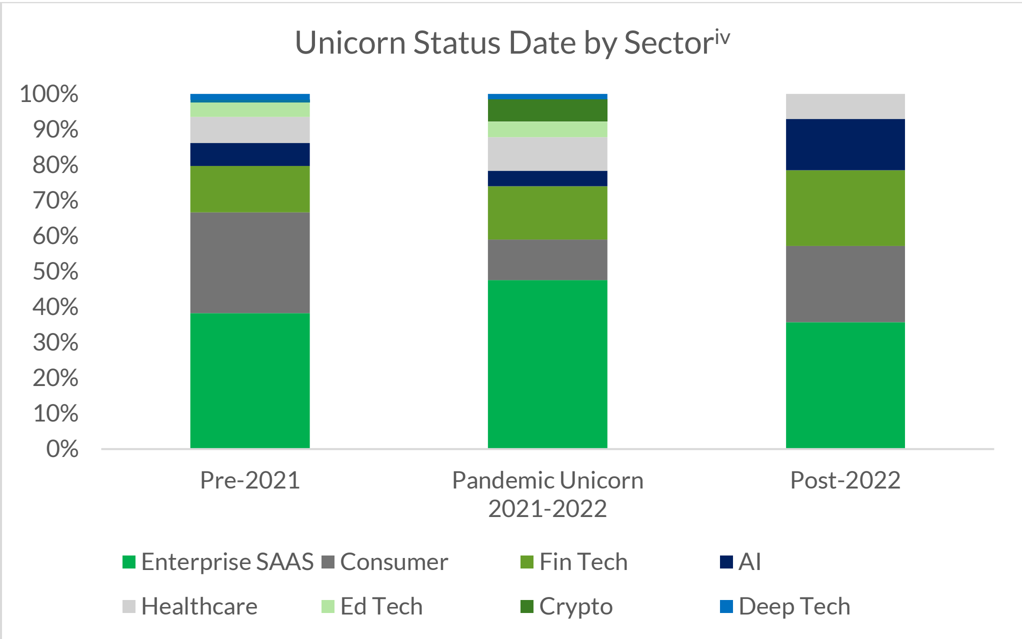


Source: Data provided by Pitchbook, 'Q1 2024 Pitchbook – NVCA Venture Monitor'; data excludes pharma and biotech companies. 2024 data as of March 31, 2024.

We classified 28% of the names as "PE Targets," which in our opinion have the hallmarks of companies that could be interesting targets for the increasing number of buyouts of venture-backed businesses. During the inflated valuation period of 2021 and 2022 where roughly 75% of the "PE Targets" raised their unicorn round at 20x+ revenue multiples, the multiples private equity firms were willing to pay tended to be far lower. However, today PE firms on average are paying in line with public SaaS revenue multiples, both valuing companies at around a 5x revenue multiple.[viii] Given the $1,200B in global dry powder in Buyout funds, and $448B raised by buyout specialists in 2023, the increasing number of PE Targets in this collection of Unicorns could be fertile hunting grounds for those funds to deploy capital. In fact, today over 20% of VC exits are to buyout and we are already seeing an increased pipeline in our own Tech Buyout funds.[vii]

In this dataset, 19% of companies still have "Unicorn Potential," but we believe they may not be considered Unicorns if they were to raise today based on their scale. Upon a closer look into this group of fast-growing Unicorn companies, it was interesting to find that many of these companies have fallen in value and roughly 50% are not marked as Unicorns today using our outside valuations methodology. These companies can still regain Unicorn status in our view, as long as they continue to compound and maintain high levels of revenue growth as they cross >$100M revenue scale.

OBSERVATION #3: UNICORN SECTORS ARE NOT ALL CREATED EQUAL



Unsurprisingly, the largest proportion of Unicorns sits within the enterprise SaaS sector, accounting for nearly 40% of all pre-, post-, and pandemic Unicorns and reflective of the overall VC funding environment. We saw an uptick across the VC landscape in companies reaching Unicorn status during the inflated valuation period of 2021 and 2022 (prior to 2021 there were only 387 Unicorns total), and Crypto was the biggest beneficiary. However, post-2022, Crypto and EdTech have not seen a Unicorn minted, underscoring the current lower valuations in those sectors. AI, however, seems to have taken the place of these sectors, seeing a large increase in Unicorn-crowned companies post-2022. If we consider the entire CB Insights list for AI Unicorns post-2022, they now account for about 20% of new Unicorns.[iii] We acknowledge there is also some overlap with the non-pure AI play names as well, as many of the newly minted Unicorns in categories such as enterprise SaaS today also have some sort of AI angle, so the total percentage of new Unicorns that have AI products is likely significantly higher than 20%.

CONCLUSION

All of the methods we have used to determine Unicorn value have converged at a similar answer, which is that about half of the Unicorn population could be dehorned. While historically reaching Unicorn status indicated a promising level of success, with the current herd you may need to take a closer look under the hood and see if they have the true fundamentals of a Unicorn.

However, notwithstanding the large fluctuations in valuations for Unicorns, many of these companies have remained resilient (particularly in AI) and could eventually recover to or surpass their peak valuations as they reaccelerate growth. We are particularly excited about the secondary opportunity in these names as expectations in the secondary market have come down from peak levels. We are further encouraged that tech innovation continues to drive as fast as ever, and new Unicorns are now being created again as the market recovers.

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Footnotes

i. “Welcome Back to the Unicorn Club, 10 Years Later”, Cowboy Ventures. January 18, 2024. (Cowboy Ventures | Welcome Back to the Unicorn Club, 10 Years Later)

ii. “Unicorns, Undercorns, And Horses: A Guide To The Nonsense”, Crunchbase. April 10, 2019. (Unicorns, Undercorns, And Horses: A Guide To The Nonsense (crunchbase.com))

iii. “The Complete List Of Unicorn Companies”. CBInsights, March, 2024. (The Complete List Of Unicorn Companies (cbinsights.com))

iv. “Industry Ventures Proprietary Data”. Industry Ventures, March, 2024.

v. “Hyperscalers Report Q1 + Early Look at Software Reports”, Clouded Judgement. May 3, 2024. (Clouded Judgement 5.3.24 - by Jamin Ball (substack.com))

vi. “The BVP Nasdaq Emerging Cloud Index”. Bessemer Venture Partners, May, 2024. (BVP - Overview)

vii. “GLOBAL PRIVATE EQUITY REPORT 2024”, Bain Capital. May 8, 2024. (Bain_report_global-private-equity-report-2024)

viii.“Q1 2024 Pitchbook –NVCA Venture Monitor”, Pitchbook. March 31, 2024