A WORD FROM J.P. MORGAN
Our views on venture

Europe's economic outlook is improving just as elections are stirring up market volatility.

Most macroeconomic indicators in Europe point to some improvement after muted growth in late 2023 and early 2024. In June, the European Central Bank (ECB) made its first rate cut in almost five years, lowering policy rates by a quarter point to 3.75%. Even though inflation is likely to remain above target into next year and visibility is low, we expect two additional cuts in 2024 and five next year as the ECB has entered the "dialling back" phase of its restrictive stance on monetary policy.

Unexpected election outcomes are a larger-than-usual risk to the outlook this year. The recent political developments in France caused French sovereign bond spreads to experience historic widening. While the flow-through into economic growth is likely to be limited, it is a recent reminder to founders and investors to be prepared for a wide range of market events and scenarios. This could take the form of higher rates, a commodity or foreign exchange shock, or politically or geopolitically induced volatility.

Signs of recovery are emerging across the Europe venture capital ecosystem.

Following a significant pullback over the past two years, it is encouraging to see improving activity across the Europe, Middle East, and Africa (EMEA) venture capital ecosystem. In most aspects, conditions have returned to pre-pandemic levels. Deals occurring at the Series A level are looking robust, with both sizes and valuations back above 2021 peaks. On the other hand, later-stage companies are attracting less funding and challenged to maintain valuations attributed at previous rounds.

UK-, European Union-, and US-based venture capital firms remain focused on deploying capital as well as nontraditional venture capital, such as corporate venture capital (CVC) funds. This activity will be important to watch within the deep tech and artificial intelligence (AI) space as these sectors appear to be attracting a more diverse investor base. Corporates are keen to understand which technologies may enhance or disrupt their business models, and investing in those technologies may serve as a natural hedge.

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Overall, as venture investment activity continues to recover, funding for EMEA venture funds is following suit. The number and size of venture funds raised have been on an upward trend since the first quarter of 2023, implying a return to better times for EMEA venture investors. Furthermore, the number of venture megafunds (funds over $1 billion) has also increased over the same time period.

From a regional perspective, it is notable that startups out of the Nordic region have consistently performed well. Despite the Nordics being a relatively small section of EMEA's venture ecosystem, the quality of what has been created, commercialized, and globalized in the region has been as good as anything in Europe. With the rise of climate tech, this trend should continue. Outside of the Nordics, we have seen city centres with strong universities such as Manchester, Edinburgh, and Zurich also produce companies rich in intellectual property.

The exit environment is on the road to recovery with initial public offerings (IPOs) restarting and mergers & acquisitions (M&A) remaining integral.

IPOs have had their strongest start to the year since the heights of 2021. In Europe alone, issuance has been more than double the same period in 2023. Strong global investor demand and supportive aftermarket performance have helped create momentum for IPOs. In combination with a clearer outlook for interest rates and regional stock markets

hitting all-time highs, there has been increased engagement from sponsors and founders on exit opportunities within the public markets.

In addition to IPOs, equity capital markets continue to be very busy in general. There has been a surge of activity in blocks, rights issues, and convertibles over the past four to six months. At the same time, M&A activity is solid, with notable cross-border demand. In the first few months of the year, nearly half of the top 30 acquirers of EMEA-based startups were US based.

When evaluating an equity raise or public listing, important considerations for founders include where the relative comparable set trades best and where the deepest pools of capital are found. US markets have the deepest pools of capital and trading liquidity, so it is natural that the number of conversations with international companies to list on US exchanges has increased with the US IPO market restarting. In some cases, the best option could be closer to home. Europe and other listing venues are fully viable to complete a deal; for example, both Puig and CVC listed well and have traded positively.

Private capital markets remain active.

The trends observed across private capital markets in the US are carrying over to Europe, as Q2 2024 saw a higher dollar volume of deals than Q2 2023 even though deal counts were lower. This relates to late-stage AI & machine learning (ML) startups, which saw sizeable raises in Q2. The quarter has also seen a pickup in activity from fintech companies, which we expect to accelerate through the year.

Investors remain focused on paths to profitability, although unique and strong growth stories are still being well rewarded.

European companies continue to attract global investors with strong participation from US venture capitalists.

Venture debt as a potential source of capital should be considered carefully and in a long-term context.

More venture debt providers have come into the European market, including both debt funds and banks that have widened their debt aperture. This has increased awareness and availability of nondilutive capital such as venture debt. The ongoing pressure on prior-round valuations has increased its attractiveness as a potential source of capital.

But like equity partners, it is important for founders to consider venture debt providers as a long-term relationship. It is critical to choose a partner you can trust over time and one that is vested in the long-term success of your company—not just in securing the best terms available at this point in the cycle.

Regulatory developments remain top of mind, especially in fast-growing sectors.

The fastest-evolving sectors are those receiving the highest level of investment: AI and climate tech. Within AI, we are beginning to see real applications within verticals, and soon enough, the word “AI” will be akin to “software.”

To effectively regulate AI in real time, legislators need to be fluent in the industry and part of the change, or there will be a consistent lag, which presents risks for unintended consequences. In the near future, we expect large corporations across industries to start incorporating the latest developments in AI & ML. This will likely test the applicability and suitability of existing AI regulation, leading to a further refined take on the subject and likely closer regulatory alignment across geographies.

Outside of AI, fraud continues to be a growing concern with regulators and tech companies alike. Reducing friction for customers is a key element in growing market share and encouraging adoption of new technologies; yet at the same time, it attracts bad actors who exploit weaknesses.