WILSON SONSINI ECP

EMERGING COMPANIES PRACTICE

ecp.wsgr.com

THE ENTREPRENEURS REPORT

PRIVATE COMPANY FINANCING TRENDS

From the Wilson Sonsini Database:

FINANCING TRENDS FOR FULL-YEAR 2023

Key Developments in This Report

Seed and Series A Valuations End 2023 at All-Time Highs

Ending 2023 on a positive note, Seed and Series A valuations hit record peaks in Q4. Seed valuations are starting to look like Series A valuations five years ago and hint that the upward trend might continue into 2024. However, despite early-stage surges, Series C and later valuations remained relatively flat throughout 2023.

See p. 4

Fundraise Amounts Finish the Year Up Across the Board

Despite considerable variability in 2023, fundraise amounts across all stages finished the year with quarter-over-quarter increases. Record raise amounts for Seed and Series A, along with an upward trend for later rounds, suggest a tepid but positive outlook for 2024 fundraise amounts.

See p. 5

Investors Continue to Receive Favorable Deal Terms

The prevalence of down rounds remains above historical levels but may have peaked in 2022. Any shift toward investor-favorable terms in 2023 was largely confined to down rounds.

See p. 6

Convertible Notes Demand Higher Interest Rates and Reduced Maturity Periods

Even in the age of SAFEs, convertible notes remain popular and Q4 2023 saw the highest median raise amounts for notes for the year. Significantly, the trend toward shorter maturity periods, particularly in the pre-Seed stage, highlighted investors' expectations of follow-on equity rounds in 2024.

See p. 8

Seth Helfgott

Ed Yip

2024 VENTURE OUTLOOK

Wilson Sonsini's **Seth Helfgott** in Conversation with Norwest's **Edward Yip**

Seth Helfgott is a partner in the SOMA office of Wilson Sonsini, where he focuses on corporate and securities law, including start-ups, venture capital transactions, mergers and acquisitions, and corporate governance matters.

Ed Yip joined Norwest Venture Partners in 2012 to partner with founders who are building the next generation of companies in the consumer internet space. As a partner, he makes Seed-, early-, and late-stage investments in a range of areas including commerce, marketplaces, hardware-enabled services, and fintech.

SH: Valuations remain near historic highs for early-stage start-ups while many later-stage companies are facing depressed valuations and down-rounds. Do you expect these trends to continue in 2024?

EY: Cautiously optimistic, [but] we still think that the mid- to late-stage venture market is going to be slow. The valuation reckoning for companies that raised large growth rounds in 2020-2021 will accelerate and we'll see more recaps, down rounds, etc., this year. There will still be good companies that will raise mid/late-stage rounds and with all the money on the sidelines remaining, they'll raise large rounds at high valuations. However, that stage of the market will overall still be slow. The early stage (pre-Seed, Seed, Series A) side of the market will be active, and valuations will continue to come down here (excluding AI companies). We're continually active on the growth equity side of our business (EBITDA profitable companies) and continue to see opportunities there.

SH: You focus on consumer-facing companies. What challenges and opportunities do you anticipate in that space this year?

EY: Consumer is still a challenged sector. User acquisition continues to be expensive and performance marketing consumer acquisition costs will rise with mature platforms and increasing big brand budgets. With the market now emphasizing profitability, direct-to-consumer companies are finding it increasingly difficult to grow and gain marketing leverage to prove a path to profitability. Successful consumer companies will have strong organic, word-of-mouth growth potential, network effects, high retention/repeat usage, high product margins, and omnichannel platforms (digital and offline). However, there are reasons for optimism in the space. GenZ and GenAlpha consumers are growing as a larger share of the market and have different product preferences as opposed to older generations. We'll begin to see "updated" applications and utilities that reflect this shift. Also, the next generation of consumer companies will likely find ways to leverage cheaper growth from newer social platforms.

SH: Many start-ups raised their last round of capital in 2021 or 2022. How are you advising founders approaching the end of their runway?

EY: It definitely depends on the growth profile. If growth has been strong and efficiency has been improving, there is still a lot of venture money on the sidelines looking to invest. Valuation multiples may come down as investors are more focused on public multiples in the later stage, but the top-tier companies will be able to raise. Companies that haven't grown into their valuations should start thinking early about plan B – either an internal raise, building a deeper relationship with potential acquirers, or better yet – push for profitability so you can control your own destiny.

SH: What advice do you have for entrepreneurs hoping to raise their first round of venture capital this year?

EY: The seed market is still healthy and active, so a lot of the same advice applies. Focus on a problem/space that you're deeply passionate about and have experience in, make sure it's a big Total Addressable Market (so that if it works it can drive big venture returns), and have a strong and detailed product vision so there's a business model that has potential for high margins, retention, and operational leverage over time.

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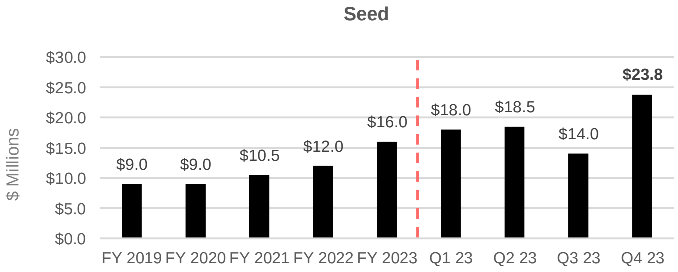
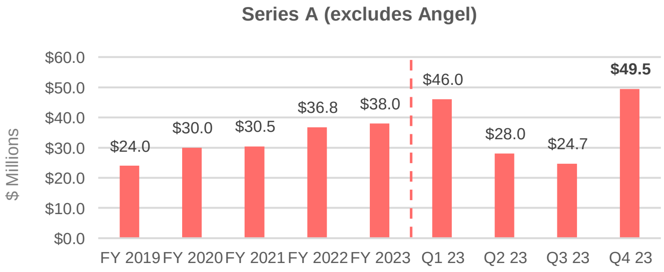
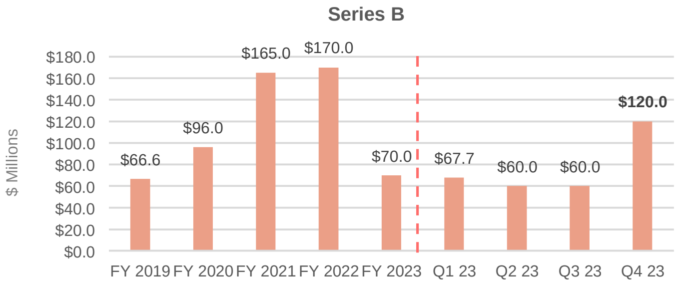
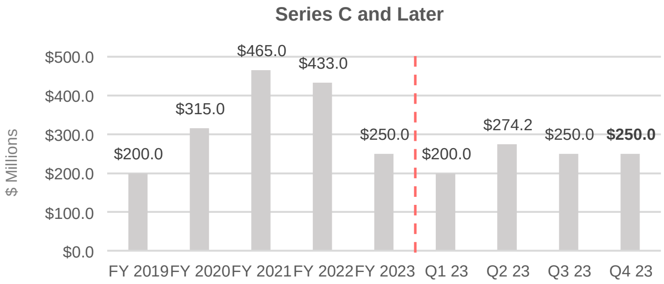
PRE-MONEY MEDIAN VALUATIONS*

Seed and Series A Valuations End 2023 at All-Time Highs









Driven in part by investors hoping to buy a piece of the next big artificial intelligence start-up, median Seed valuations shot up to nearly $24 million in Q4 2023.

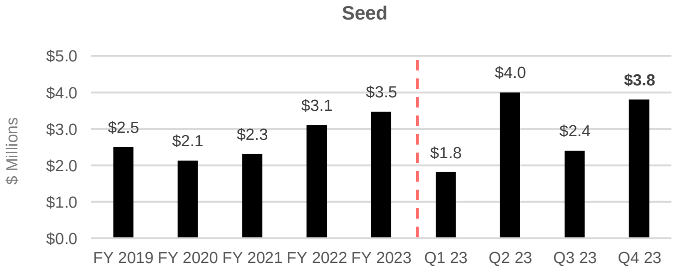
Current Seed valuations are starting to look a lot like Series A valuations from 2019, a trend that could continue into 2024 as firms look to deploy more sidelined dry powder into early-stage companies.

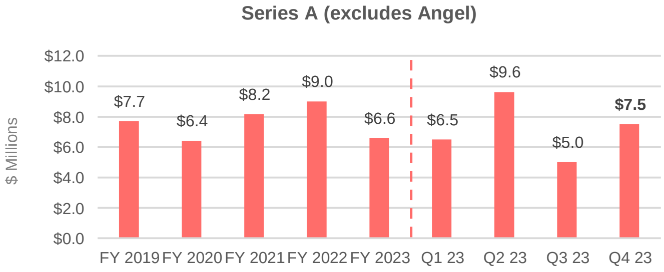
Valuations were also up in Q4 2023 at the Series A and Series B stages while Series C and later valuations were mostly flat throughout 2023, a trend that is likely to continue until IPOs become a more viable exit possibility for later-stage technology companies.

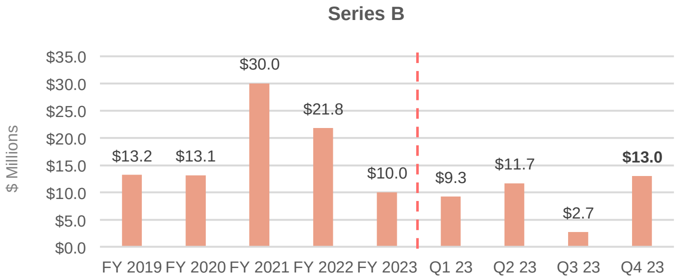
* For a quarter-by-quarter breakdown of pre-money median valuations dating back to Q1 2021, see the Appendix on page 15.

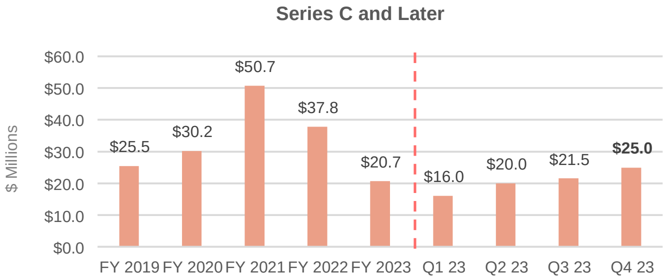
EQUITY FUNDRAISE MEDIAN AMOUNTS*

Fundraise Amounts Finish the Year Up Across the Board







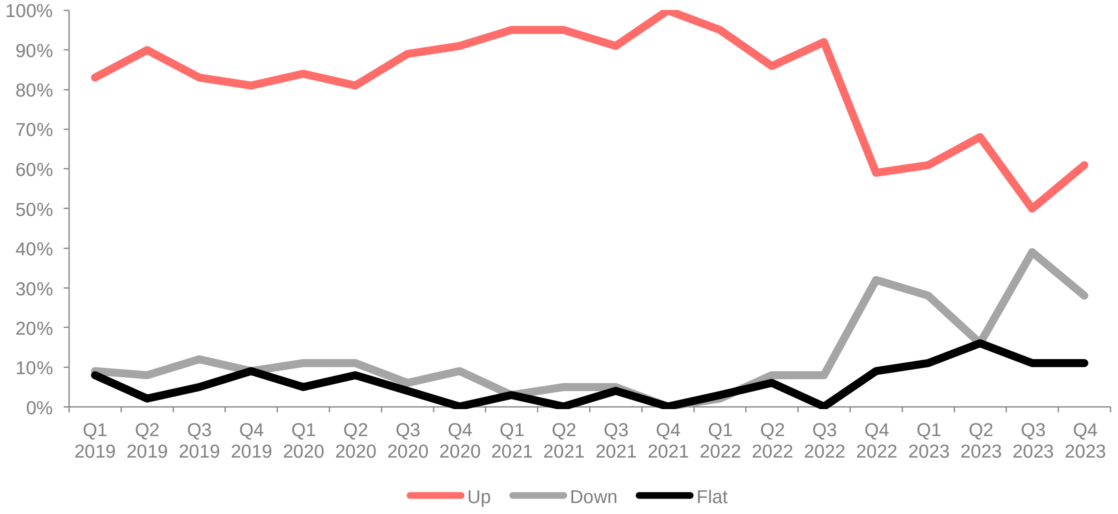


Raise amounts in 2023 fluctuated widely, with a couple of quarterly all-time highs (Seed and Series A in Q2 2023) alongside lows not seen since 2019 (Series B in Q3 2023 and Series C and later in Q1 2023). However, raise amounts at all stages managed to end the year with quarter-over-quarter increases.

Whether the whiplash will continue into 2024 remains to be seen, but later-stage companies may find comfort in the slow but consistent increase in Series C and later raise amounts over the last four quarters.

* For a quarter-by-quarter breakdown of equity fundraise median amounts dating back to Q1 2021, see the Appendix on page 15.

Down Rounds Decrease but Still Make Up Nearly 30% of Transactions



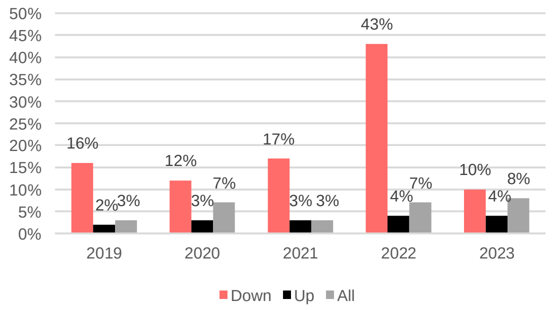
2023 was a bit of a rollercoaster ride for those tracking down round trends. After a worrisome Q3, which saw down rounds making up nearly 40% of transactions, the percentage of companies raising an up round in Q4 increased slightly but remains well below 2021 levels.

For now, the prevalence of up, flat, and down rounds at the end of 2023 is looking very similar to the landscape in Q4 2022. Whether this trend continues into 2024 will likely depend on whether Seed- and Series A-stage companies that were fortunate enough to raise money recently in 2022 and 2023 are able to maintain enough momentum to justify increasing valuations.

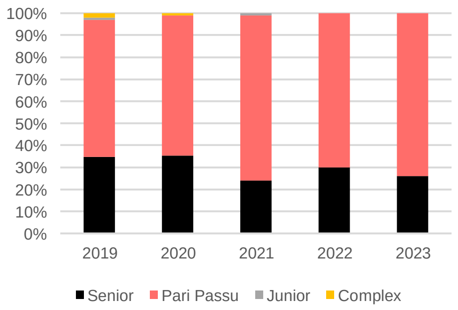
EQUITY FINANCING DEAL TERMS*

Some Investor-Friendly Terms Remain Common but Are Mostly Limited to Down Rounds

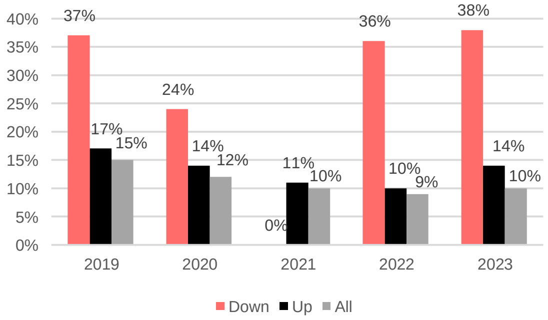
Deals with Pay to Play
(Series B and Later Financings)



Liquidation Preferences
(Series B and Later Financings)



Participating Liquidation
(All Preferred Stock Financings)



After a somewhat dramatic increase in investor-favorable terms in 2022, this year started with an open question of whether this trend would solidify into a more investor-favorable "new normal" with respect to equity deal terms. 2023 data indicates, however, that any industry-wide shift remains mostly limited to down rounds. Participating preferred stock, which provides more potential upside for investors when a company does well, continues to be a common feature of down round investments, but remains relatively rare in up and flat rounds.

Conversely, "pay to plays," a feature which can dilute or adversely affect existing investors that decline to invest additional capital, were less common even in 2023's down rounds after reaching record levels in 2022.

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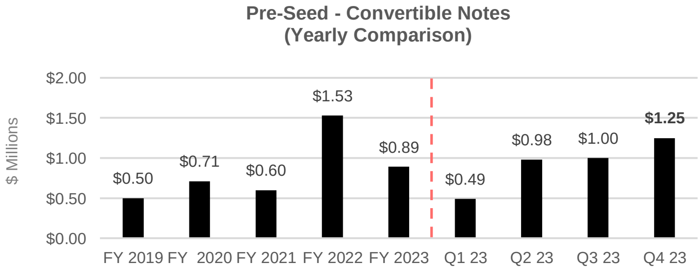
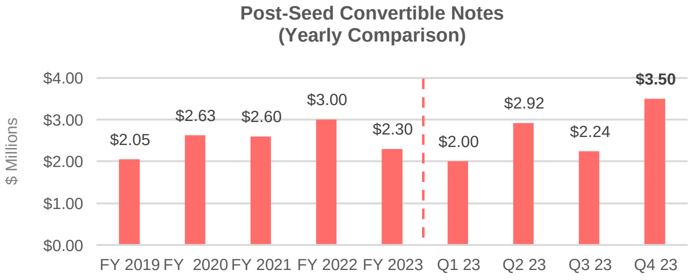
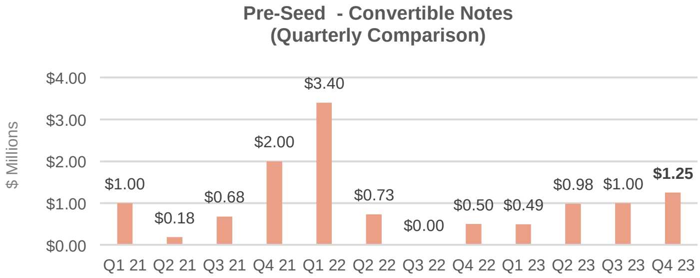
* For a more detailed summary of private company financing deal terms, see the Appendix on page 16.

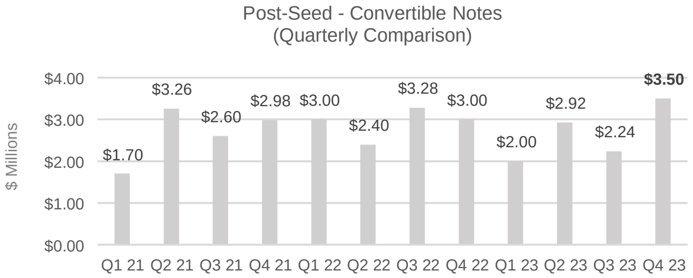
CONVERTIBLE NOTE MEDIAN RAISE AMOUNTS

Pre-Seed and Post-Seed Convertible Notes Raises Trend Upwards









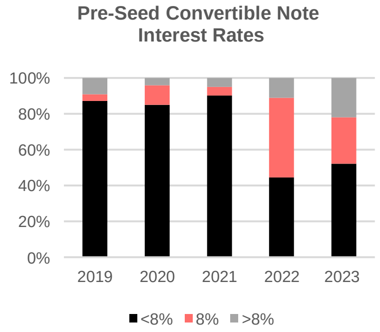
As SAFEs have become more common over the past decade, some commentators predicted that convertible notes would soon fall out of favor with investors and be supplanted by the simpler SAFE as the preferred non-equity investment instrument for bridge rounds.

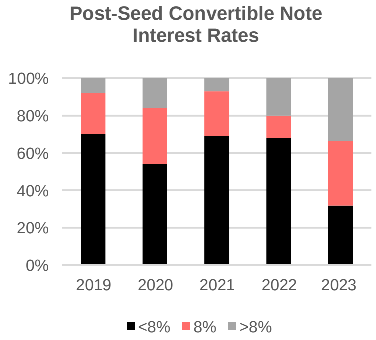
Such predictions appear to be premature, with convertible notes making up 48.5% of bridge rounds in 2023 (compared with 43% in 2022).

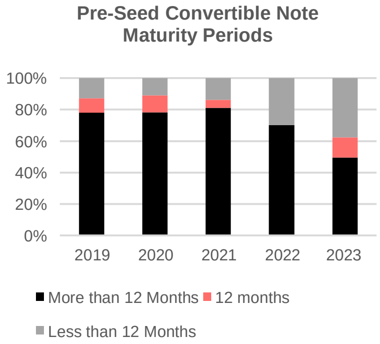
Both pre-Seed and post-Seed convertible notes ended 2023 on a high note, although pre-Seed raise amounts remain well below the peak of late 2021/early 2022.

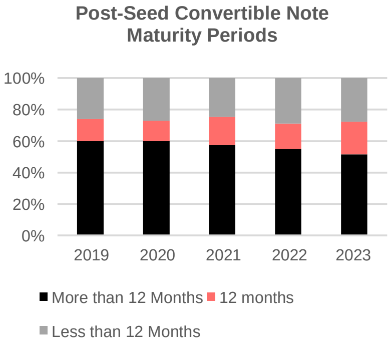
CONVERTIBLE NOTE DEAL TERMS*

Note Interest Rates Are Up, Maturity Periods Are Down









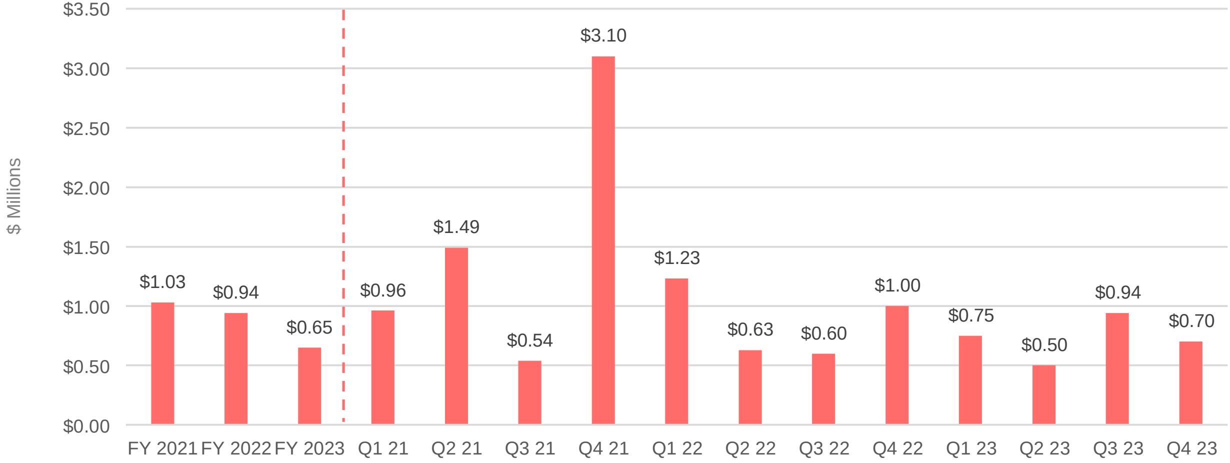
Maintaining the trend that started with the Federal Reserve's interest rate increases in March 2022, 48% of pre-Seed and 68% of post-Seed convertible notes had higher-than-typical interest rates of 8% or higher in 2023. While note interest rates are not directly correlated to the federal funds rate and are perhaps better seen as a proxy for an investor's risk tolerance, start-ups should watch closely to see if the Federal Reserve's anticipated 2024 rate decreases result in any relaxation of aggressive interest rate terms this year.

The shift towards shorter maturity periods for convertible note rounds continues but in 2023 was more pronounced at the early pre-Seed stage, where roughly half of notes had maturity dates of 12 months or less. The message to young companies is clear: investors are expecting swift progress toward an equity round, often within a year or less of a pre-Seed investment.

* For a more detailed summary of convertible note deal terms, see the Appendix on page 17.

SAFEs

SAFE Median Raise Amounts Remain Under $1 Million



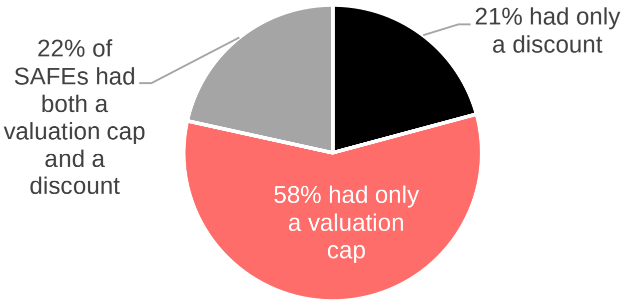
The median amount raised in SAFE financings in Q4 2023 decreased to $700,000 and remained at or below $1 million for the seventh consecutive quarter.

Despite the larger SAFE rounds seen a couple of years ago, SAFEs have returned to their pre-pandemic status as a tool generally limited to very early-stage funds and angel investors.

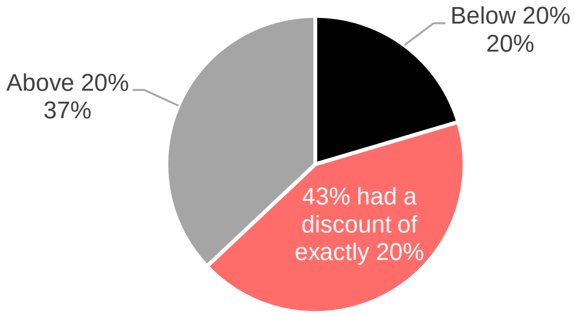
SAFEs

SAFE Investors Stick to Standard Terms

Valuation Caps and Discounts



Discount Rates



In 2023, SAFE terms remained largely in line with those seen in 2022, with a few minor variations. Forty-three percent of 2023 SAFEs included a discount, a negligible increase from 38% in 2022. Meanwhile, valuation caps were incorporated in 80% of SAFEs, down from 90% in 2022, with a median valuation cap of $15 million. The minor decrease in valuation caps is a data point to watch going into 2024 and may suggest growing investor uncertainty around early-stage valuations.

As a complement to the Wilson Sonsini deal data contained in this report, the firm recently analyzed more than 300 SAFEs issued in 2023 and found that 98% of those SAFEs were on a variant of Y-Combinator's form of SAFE. This may explain why SAFE terms, unlike those of convertible notes, remain somewhat standardized and have not materially shifted to become more investor-favorable over the past two years.

The Corporate Transparency Act's Beneficial Ownership Information Reporting Requirements

The U.S. Department of the Treasury's Financial Crimes Enforcement Network's (FinCEN's) regulations on Beneficial Ownership Information Reporting Requirements (BOI Requirements) went into effect on January 1, 2024. This set of regulations constitutes a significant change by requiring companies to affirmatively disclose beneficial ownership information to FinCEN. It is intended to better enable law enforcement to investigate crime by minimizing anonymous business activity.

When Must a Report Be Filed?

Reporting *companies created or registered before January 1, 2024*, have until January 1, 2025, to comply with these regulations. FinCEN has indicated it will provide additional guidance in the coming months, which may clarify some of the obligations under these reporting requirements. Additionally, the obligation to file updated reports does not begin until the initial report has been filed.

Reporting companies *created or registered in 2024* will have 90 calendar days after creation or registration, as applicable, to comply.

For more information on the BOI regulations, continue reading or please contact Wilson Sonsini attorneys at CTA@wsgr.com.

The Corporate Transparency Act's Beneficial Ownership Information Reporting Requirements (Cont.)

Which Entities Are Required to Report?

Reporting Companies are nonexempt domestic and foreign entities that meet one of the following definitions:

- **Domestic Reporting Companies:** LLCs, corporations, and other entities created by filing a document with a secretary of state or similar office under state or tribal law
- **Foreign Reporting Companies:** Entities formed under the laws of a foreign country and registered to do business in any state or tribal jurisdiction by filing a document with a secretary of state or similar office under state or tribal law
- **Sole proprietorships, certain trusts, and general partnerships** are generally not created by filing a document with a secretary of state or similar office, and thus are not required to file

Which Entities Are Exempt?

While the general definitions of "domestic reporting company" and "foreign reporting company" are extremely broad, FinCEN has provided 23 enumerated exemptions will exclude a large number of businesses from the filing requirements. For example:

- Securities reporting issuers (i.e., public companies)
- "Large operating companies," which are entities that (a) employ more than 20 full-time employees in the U.S., (b) reported more than $5,000,000 in gross receipts or sales to the IRS in the previous year (excluding gross receipts or sales from sources outside the U.S.), and (c) have an operating presence at a physical office within the U.S.
- Investment advisers, venture capital fund advisers, investment companies, and money services businesses
- Domestic pooled investment vehicles that are operated or advised by a bank, credit union, registered broker-dealer, registered investment company or investment adviser, or venture capital fund adviser

The Corporate Transparency Act's Beneficial Ownership Information Reporting Requirements (Cont.)

What Information Must Be Reported?

Reporting companies are required to file an initial report with FinCEN that contains the following information about the reporting company:

- full legal name
- any trade name or d/b/a name
- current address (principal place of business street address for U.S. reporting companies, and street address of the primary U.S. location for all other companies)
- state, tribal, or foreign jurisdiction of formation
- for foreign reporting companies, the state or tribal jurisdiction where the company is registered
- the IRS taxpayer identification number (TIN), including an employer identification number (EIN).

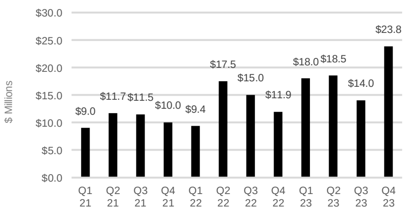
In addition, the initial report must include information about each "beneficial owner" of the reporting company, which is any individual who, directly or indirectly either:

- Owns or controls at least 25% of the ownership interests of a reporting company (assuming the exercise of granted options); or
- Directly or indirectly exercises substantial control over the reporting company by:
  - Serving as a senior officer (including President, CEO, CFO, COO, GC, or other officer who performs similar function);
  - Holding authority to appoint/remove any senior officer or a majority of directors (or similar body);
  - Directing, determining or having substantial influence over important decisions (e.g., strategic decisions re: business activities; major investments or expenditures; issuing equity; incurring significant debt; approving operating budget; sale, lease mortgage, transfer or principal assets; geographic focus); or
  - Holds any other form of substantial control.

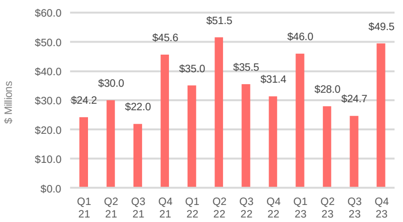
Appendix – A Quarterly Look-Back on Equity Valuations and Raise Amounts

Pre-Money Median Valuations

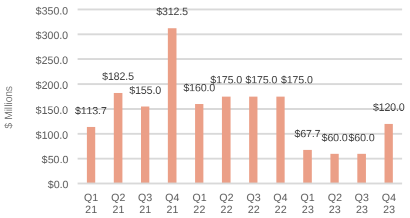
Seed



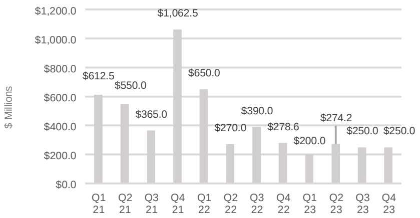
Series A (excludes Angel)



Series B

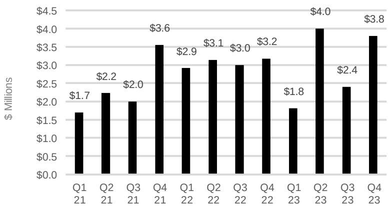


Series C and Later

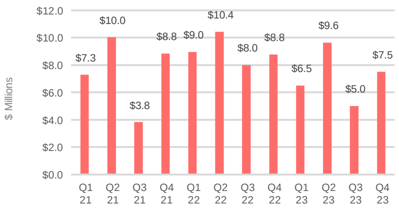


Equity Fundraise Median Amounts

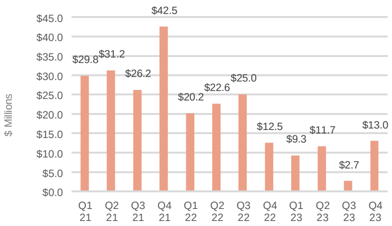
Seed



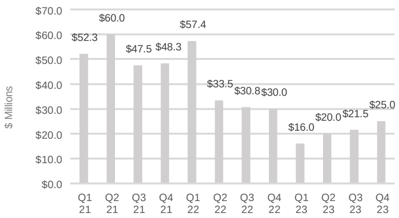
Series A (excludes Angel)



Series B



Series C and Later



Appendix – Private Company Financing Deal Terms (Wilson Sonsini Deals)

	2019 All Rounds[2]	2020 All Rounds[2]	2021 All Rounds[2]	2022 All Rounds[2]	2023 All Rounds[2]	2019 Up Rounds[3]	2020 Up Rounds[3]	2021 Up Rounds[3]	2022 Up Rounds[3]	2023 Up Rounds[3]	2019 Down Rounds[3]	2020 Down Rounds[3]	2021 Down Rounds[3]	2022 Down Rounds[3]	2023 Down Rounds[3]
Liquidation Preferences - Series B and Later															
Senior	35%	35%	24%	30%	26%	30%	32%	23%	26%	20%	63%	56%	50%	64%	38%
Pari Passu with Other Preferred	63%	63%	75%	70%	74%	68%	67%	76%	74%	80%	37%	44%	50%	36%	62%
Junior	1%	0%	1%	0%	0%	1%	0%	1%	0%	0%	0%	0%	0%	0%	0%
Complex	2%	1%	0%	0%	0%	2%	1%	0%	0%	0%	0%	0%	0%	0%	0%
Participating vs. Non-Participating															
Participating - Cap	5%	4%	4%	3%	2%	5%	6%	4%	3%	4%	5%	0%	0%	0%	14%
Participating - No Cap	10%	8%	6%	6%	8%	12%	8%	7%	7%	10%	32%	24%	0%	36%	24%
Non-Participating	85%	88%	90%	91%	90%	83%	86%	89%	90%	85%	63%	76%	100%	64%	62%
Dividends															
Yes, Cumulative	5%	10%[4]	5%	6%	3%	6%	10%[4]	6%	8%	6%	11%	25%[4]	0%	8%	0%
Yes, Non-Cumulative	56%	79%[4]	56%	51%	46%	67%	83%[4]	65%	57%	53%	79%	69%[4]	57%	58%	65%
None	39%	10%[4]	39%	43%	51%	28%	7%[4]	29%	35%	40%	11%	6%[4]	43%	33%	35%
Anti-Dilution Provisions															
Weighted Average - Broad	94%	95%	97%	98%	98%	99%	98%	98%	99%	100%	89%	76%	100%	100%	95%
Weighted Average - Narrow	0%	1%	1%	0%	1%	0%	2%	1%	0%	0%	5%	6%	0%	0%	5%
Ratchet	0%	1%	1%	1%	0%	0%	0%	1%	1%	0%	5%	6%	0%	0%	0%
Other (Including Blend)	1%	1%	0%	0%	0%	0%	1%	1%	0%	0%	0%	0%	0%	0%	0%
None	4%	2%	1%	1%	2%	1%	0%	0%	0%	0%	0%	12%	0%	0%	0%
Pay to Play - Series B and Later															
Yes, Pay to Play	3%	7%	3%	7%	8%	2%	3%	3%	4%	4%	16%	12%	17%	43%	10%
None	97%	93%	97%	93%	92%	98%	97%	97%	96%	96%	84%	88%	83%	57%	90%
Redemption															
Yes, Redemption	14%	13%	10%	8%	5%	17%	10%	15%	12%	4%	26%	25%	17%	7%	15%
None	86%	88%	90%	92%	95%	82%	90%	86%	89%	96%	74%	75%	83%	93%	86%

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[1] We based this analysis on deals having an initial closing in the period to ensure that the data clearly reflects current trends. Please note the numbers do not always add up to 100% due to rounding.
[2] Includes flat rounds and, unless otherwise indicated, Series A rounds.
[3] Note that the All Rounds metrics include flat rounds and, in certain cases, Seed and Series A financings as well. Consequently, metrics in the All Rounds column may be outside the ranges bounded by the Up Rounds and Down Rounds columns, which will not include such transactions.
[4] The 2020 increase in the number of transactions reported as including dividends resulted in part from a change to our reporting methodology.

Appendix – Convertible Notes – Deal Terms (Wilson Sonsini Deals)

Convertible Notes[1]	2018 Pre-Seed	2020 Pre-Seed	2021 Pre-Seed	2022 Pre-Seed	2023 Pre-Seed	2019 Post-Seed	2020 Post-Seed	2021 Post-Seed	2022 Post-Seed	2023 Post-Seed
Interest rate less than 8%	87%	85%	90%	44%	52%	70%	54%	69%	68%	32%
Interest rate at 8%	4%	11%	5%	44%	26%	22%	30%	24%	12%	35%
Interest rate greater than 8%	9%	4%	5%	11%	22%	8%	16%	7%	20%	34%
Maturity less than 12 months	13%	11%	14%	30%	38%	26%	27%	25%	29%	28%
Maturity 12 months	9%	11%	5%	0%	13%	14%	13%	18%	16%	21%
Maturity more than 12 months	78%	79%	81%	70%	50%	60%	60%	58%	55%	52%
Debt is subordinated to other debt	27%	13%	14%	40%	17%	49%	46%	48%	41%	39%
Loan includes warrants[2]	2%	4%	0%	0%	100%	8%	12%	6%	20%	22%
Warrant coverage less than 25%	100%	100%	N/A	N/A	N/A	80%	67%	0%	11%	45%
Warrant coverage at 25%	0%	0%	N/A	N/A	N/A	0%	0%	0%	0%	0%
Warrant coverage greater than 25%	0%	0%	N/A	N/A	N/A	20%	33%	100%	89%	55%
Automatic conversion into equity on qualified financing[3]	100%	100%	100%	100%	92%	96%	92%	96%	93%	88%
Voluntary conversion into equity on qualified financing[3]	0%	0%	0%	0%	8%	4%	8%	4%	7%	12%
Conversion rate subject to price cap[4]	69%	68%	71%	56%	54%	51%	36%	52%	32%	47%
Conversion to equity at discounted price[5]	68%	78%	75%	50%	88%	81%	79%	70%	78%	80%
Conversion to equity at same price as other investors	12%	13%	15%	30%	8%	11%	17%	25%	20%	10%
Discount on conversion less than 20%	18%	11%	20%	40%	14%	27%	25%	21%	29%	18%
Discount on conversion at 20%	63%	69%	60%	20%	48%	57%	46%	63%	39%	55%
Discount on conversion greater than 20%	18%	20%	20%	40%	38%	16%	29%	16%	32%	27%

[1] We based this analysis on deals having an initial closing in the period to ensure that the data clearly reflects current trends. Please note the numbers do not always add up to 100% due to rounding. Pre-Seed refers to convertible notes issued prior to the first preferred stock financing. Post-Seed refers to convertible notes issued after the first preferred stock financing.

[2] Of the 2019 post-Seed convertible notes with warrants, 71% also had a discount on conversion into equity. Of the 2020 post-Seed convertible notes with warrants, 44% also had a discount on conversion into equity. Of the 2021 post-Seed convertible notes with warrants, 100% also had a discount on conversion into equity. Of the 2022 post-Seed convertible notes with warrants, 59% also had a discount on conversion into equity. Of the 2023 post-Seed convertible notes with warrants, 55% also had a discount on conversion into equity.

[3] The 2019 median dollar threshold for a qualified financing in pre- and post-Seed convertible notes was $4M and $8M, respectively. The 2020 median dollar threshold for a qualified financing in pre- and post-Seed convertible notes was $3M and $10M, respectively. The 2021 median dollar threshold for a qualified financing in pre- and post-Seed convertible notes was $4M and $10M, respectively. The 2022 median dollar threshold for a qualified financing in pre- and post-Seed convertible notes was $7M and $10M, respectively. The 2023 median dollar threshold for a qualified financing in pre- and post-Seed convertible notes was $5M and $10M, respectively.

[4] The 2019 median price cap in pre- and post-Seed convertible notes was $9M and $35M, respectively. The 2020 median price cap in pre- and post-Seed convertible notes was $8M and $47M, respectively. The 2021 median price cap in pre- and post-Seed convertible notes was $12M and $47M, respectively. The 2022 median price cap in pre- and post-Seed convertible notes was $35M and $50M, respectively. The 2023 median price cap in pre- and post-Seed convertible notes was $20M and $45M, respectively.

[5] Of the 2019 post-Seed convertible notes that had a discount on conversion into equity, 7% had warrants. Of the 2020 post-Seed convertible notes that had a discount on conversion into equity, 7% had warrants. Of the 2021 post-Seed convertible notes that had a discount on conversion into equity, 3% had warrants. Of the 2022 post-Seed convertible notes that had a discount on conversion into equity, 17% had warrants. Of the 2023 post-Seed convertible notes that had a discount on conversion into equity, 16% had warrants.

Wilson Sonsini Methodology

- The Up/Down/Flat analysis is based on Wilson Sonsini deals having an initial closing in the period reported to ensure that the data clearly reflects current trends.
- The median pre-money valuation is calculated based on the pre-money valuation given at the time of the initial closing of the financing round. If the issuer has a closing in a subsequent quarter, the original pre-money valuation is used in the calculation of the median for that quarter as well.
- A substantial percentage of deals have multiple closings that span fiscal quarters. The median amount raised is calculated based on the aggregate amount raised in the reported quarter.

This report is based on detailed deal data provided by the firm's corporate and securities attorneys and analyzed by the firm's Knowledge Management department.

For purposes of the statistics and charts in this report, our database includes venture financing transactions in which Wilson Sonsini Goodrich & Rosati represented either the company or one or more of the investors.

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