Outlier Ventures

Investments in Blockchain August 2019

Author: Joel John

Head of Research: Lawrence-Lundy-Bryan

Executive summary

- **$23.7 Billion Raised By 3738 Blockchain Companies Since 2013**
  A total of $23.7 billion has been invested into blockchain startups in multiple financing forms including ICOs, debt, direct investments and crowd-funding since 2013. However, discounting a handful of exchanges and wallets, there hasn't been a break-out or viral application, yet. This definately isn't for lack of capital. The challenge is more about expertise and guidance at early stages, especially when it comes to areas unique to Web3 such as token design.

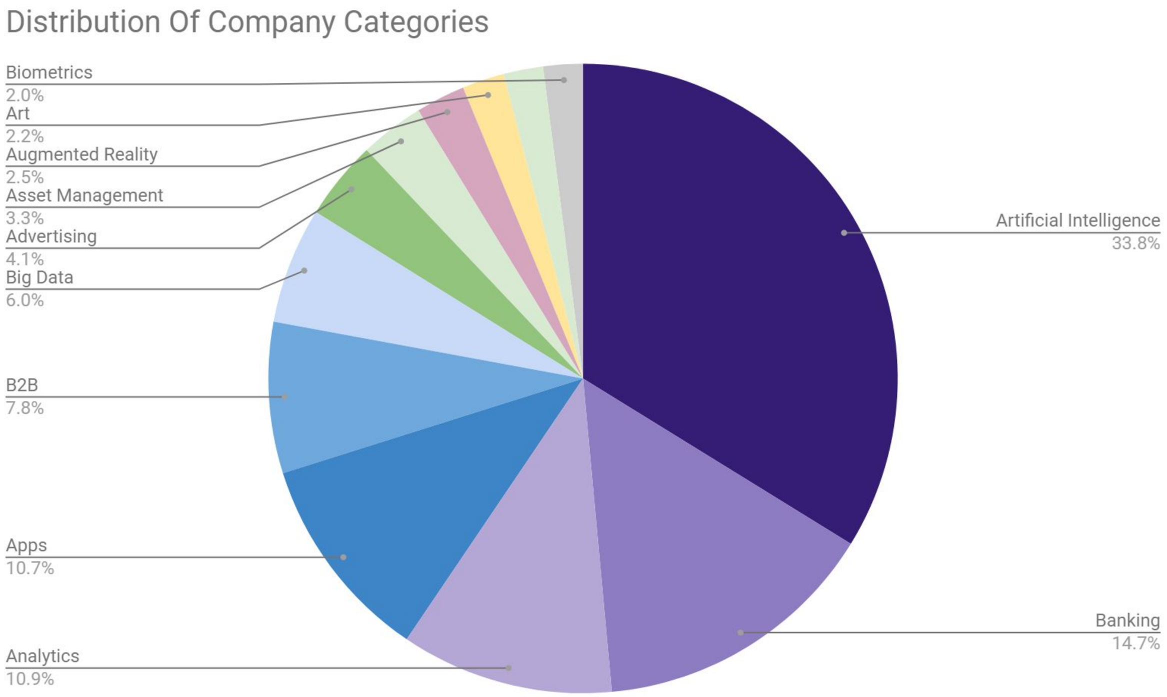
- **Early Stage Fundraising High In Count, But Follow On Rounds Few And Scarce**
  In 2019, frequency of blockchain investments will be up nine times in comparison to 2013. The number of early stage backers has increased substantially due to the massive returns from early investments in Bitcoin and Ethereum. However, the excess early financing has not converted to follow on-rounds. This suggests that while early stage funding is relatively easy, many traditional VCs are waiting for evidence of product-market fit and clearer signs of revenue before making investments.

- **75% of All Deal Flow Focused Only On Early Stage Rounds**
  Pre-seed, Seed and Angel rounds account for ~75% of all deals in the ecosystem. However, in comparison to the total figures raised by blockchain startups, early stage rounds are woefully small in size. Average seed stage rounds for blockchain firms are slightly above ~$1 million. Higher than other ecosystems. But woefully lower than series A rounds at $10 million. This has created an environment in which early stage startups are either over capitalised without product market fit or competing directly with firms with 10x more capital.

AI and FinTech Emerge As Key Focus Areas

- Bitcoin's network effects and early mover advantage meant most teams focusing on the space early on were building specifically for it.

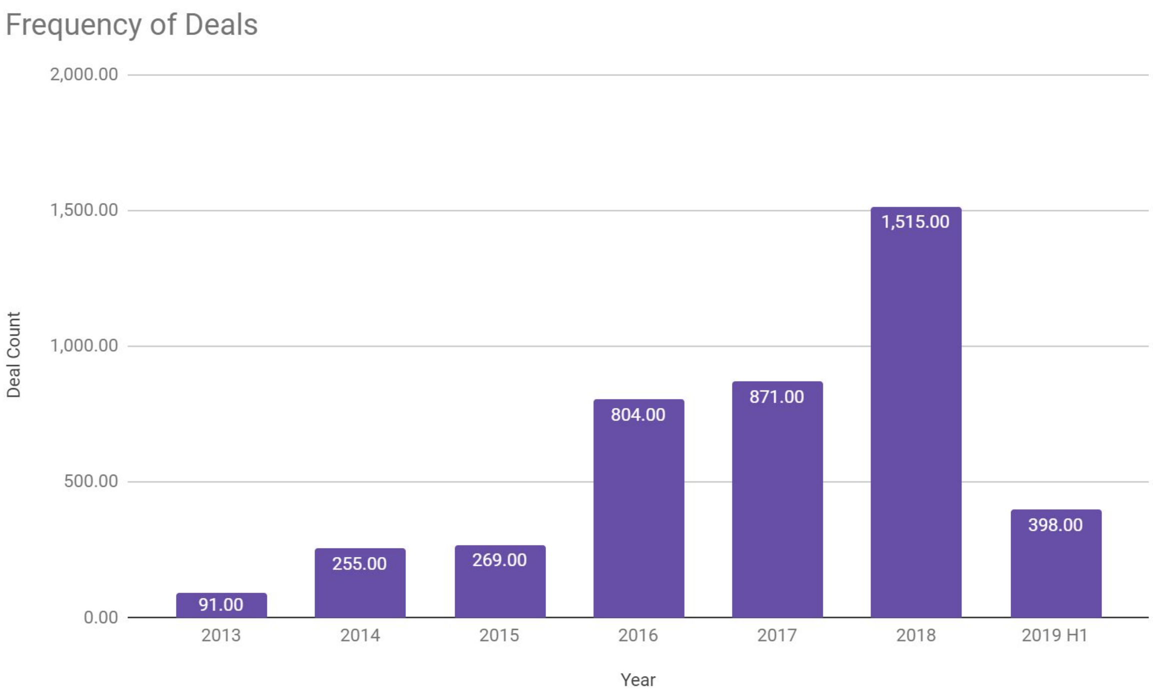
- There is a shift from focusing purely on cryptocurrency to convergence applications when considering team focus areas between 2013 to 2019. AI leads the pack, but data and ownership are not far behind.



Note : Sample size of 737 companies without focus on Bitcoin, Cryptocurrencies
Source: Crunchbase

2019 will see nine times more blockchain deals than 2013

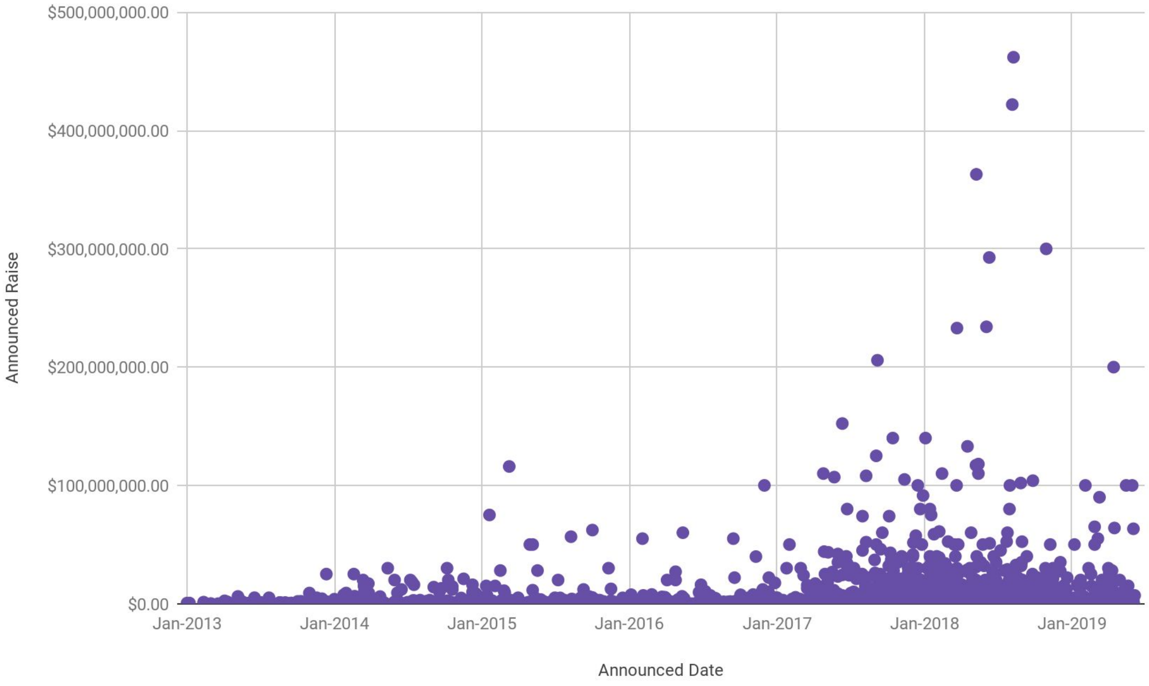
- The number of funding rounds, at seed stages has increased drastically. Providing much needed early stage financing.
- However, follow on rounds are rare. Indicating that while capital is cheap, companies are struggling to find product-market fit.



Note : Deals include ICOs, Debt, PE and Grants
Source: Crunchbase

Early stage financing is a competitive business

- The high frequency of early stage financing could indicate seed stage rounds closing quicker.
- This in turn could lead to a lack of much needed value added services investors could bring on board.
- Startups struggle with discovery, corporate collaboration and industry experience.
- The blockchain ecosystem has too many dollars chasing too few startups, which in turn solve for very niche problems.



Source: Crunchbase

Easy Capital Does Not Warrant Ecosystem Success

- 2018 witnessed roughly 130 times the funding 2013 had. And yet, in terms of a user-base, the ecosystem has not produced a similar growth pattern.
- Challenges with user experience, infrastructure, regulations and building custom tools for web 3.0 hinder the pace at which startups can grow.
- Building for blockchains is currently akin to driving a ferrari with no GPS. The fuel eventually runs out, even if the ride was enjoyable. Mentorship and guidance can redirect talent to solving the right problems

Note : Figure varies from a range of $6 billion to $24 billion depending on source.

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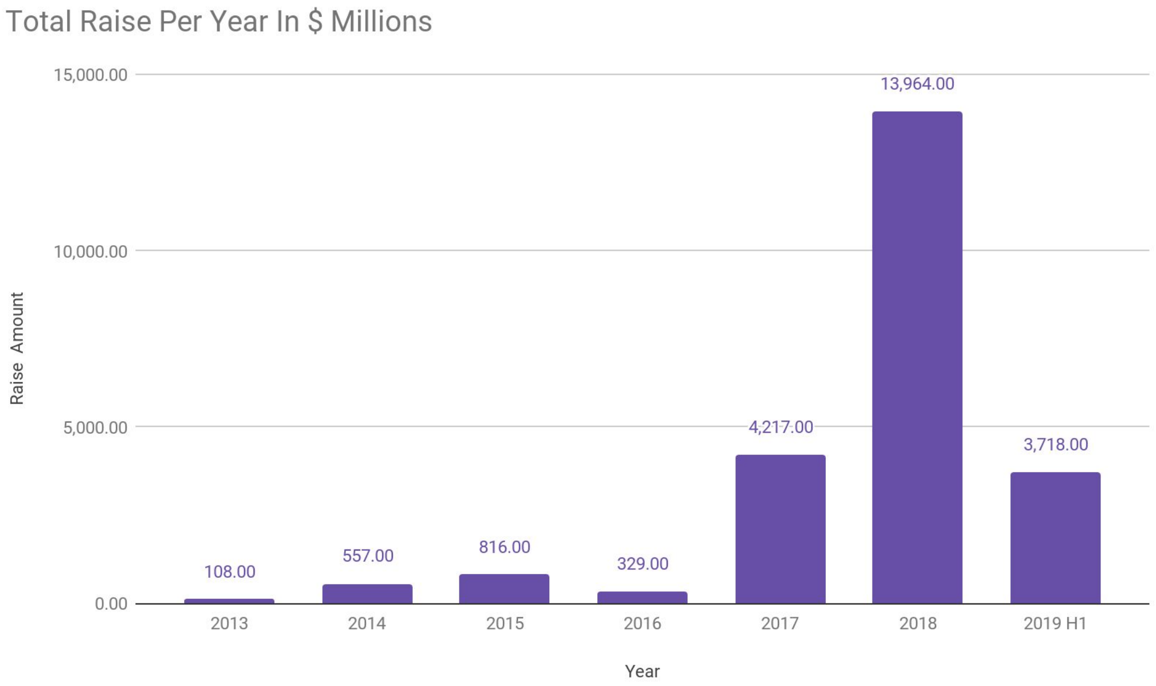
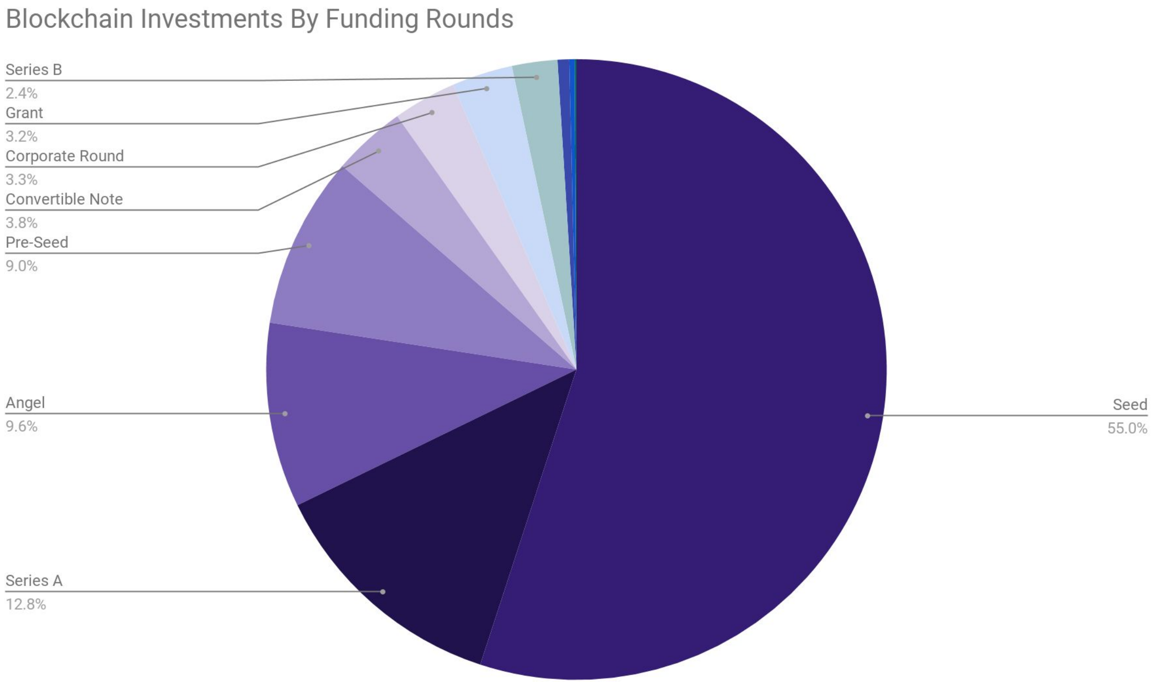


Note : Deals include ICOs, Debt, PE and Grants
Source: Crunchbase

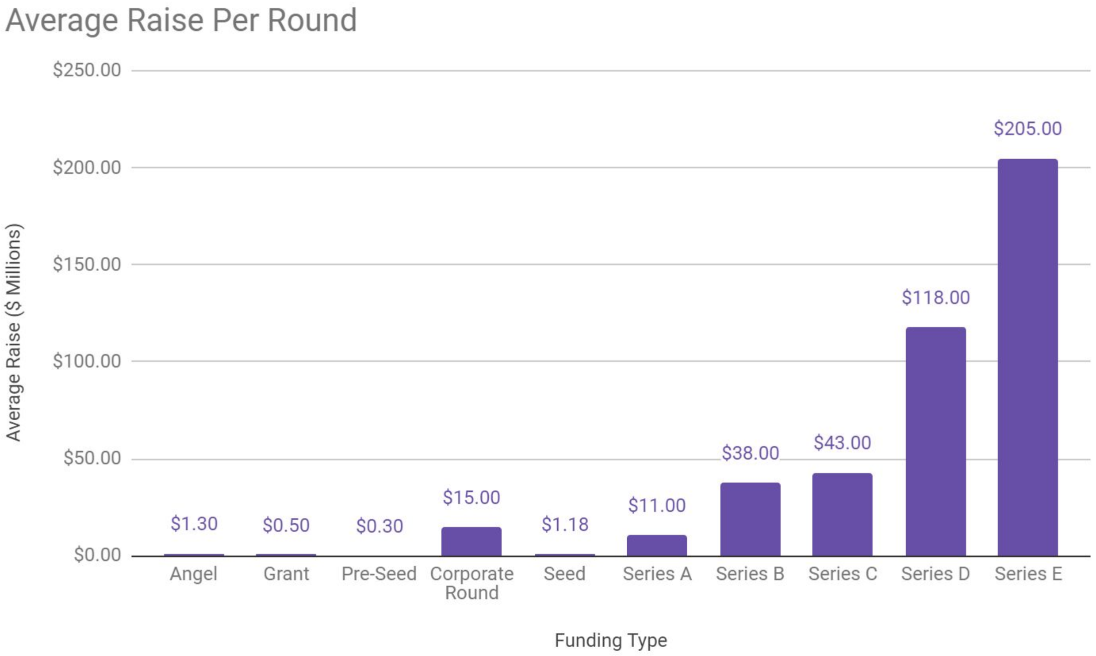
Early stage financing in the form of seed, angel and pre-seed backing constitute of 75% of all deals in the ecosystem today.



And seed stage raises are quite healthy in size

- The average seed stage firm building for blockchains raises $1.18 million. But there is a major difference between pre-seed and Series A. Seed is ~30x the amount pre-seed raises. And Series A is 10x the amount seed stage rounds are
- These incremental leaps are an indication of the extent to which investors expect a startup to grow before they are open to doing follow on rounds

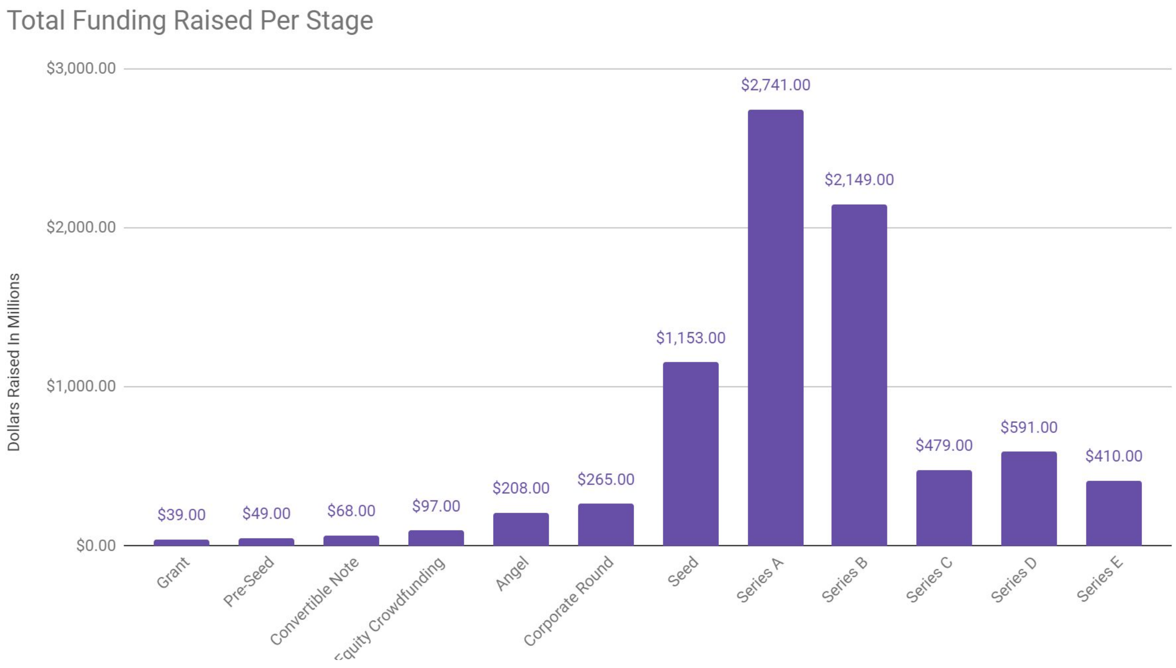
…Evolving is hard business.



Source : Crunchbase

Series A is the ultimate chasm to cross

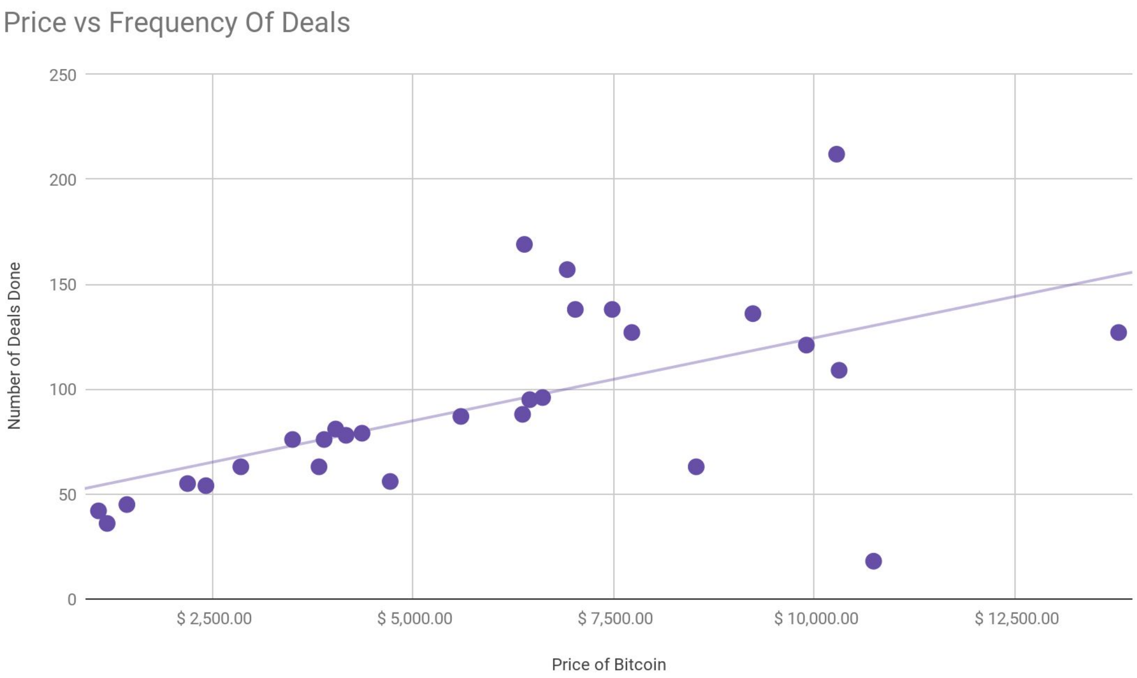
- In spite of 75% of all deals being done at the early stages, it is only at Series A that serious capital is introduced. Series A constitutes of only 12.8% of all funding rounds but attracts over 33% of all capital financing available.
- In other words, while early stage financing is in abundance, lack of expertise and product market fit could mean fewer companies go on to raise larger series A rounds. Coinbase and Circle, both exchanges are the only players to see a Series E



Source : Crunchbase

Deal frequency is still dependent on Bitcoin pricing

- Token returns determine investor appetite for backing blockchain companies. There's a reason why the ICO boom happened along-side Bitcoin's 20x rise in 2017.
- A drastic decline in Bitcoin's price could correlate with a dip in investor appetite for financing early stage, low-revenue blockchain firms.
- **Funding Is Cyclical. This adds to the uncertainties equity based token startups have.**



Source : Crunchbase, Investing.com

What’s going on?

- **Too much capital at early stages**
  Contrary to popular belief, the blockchain ecosystem’s early stage financing ecosystem is quite healthy in terms of financing. Firms that survive to see raise an average of $1.18 million, a figure that is in sync with web 2.0 peers.

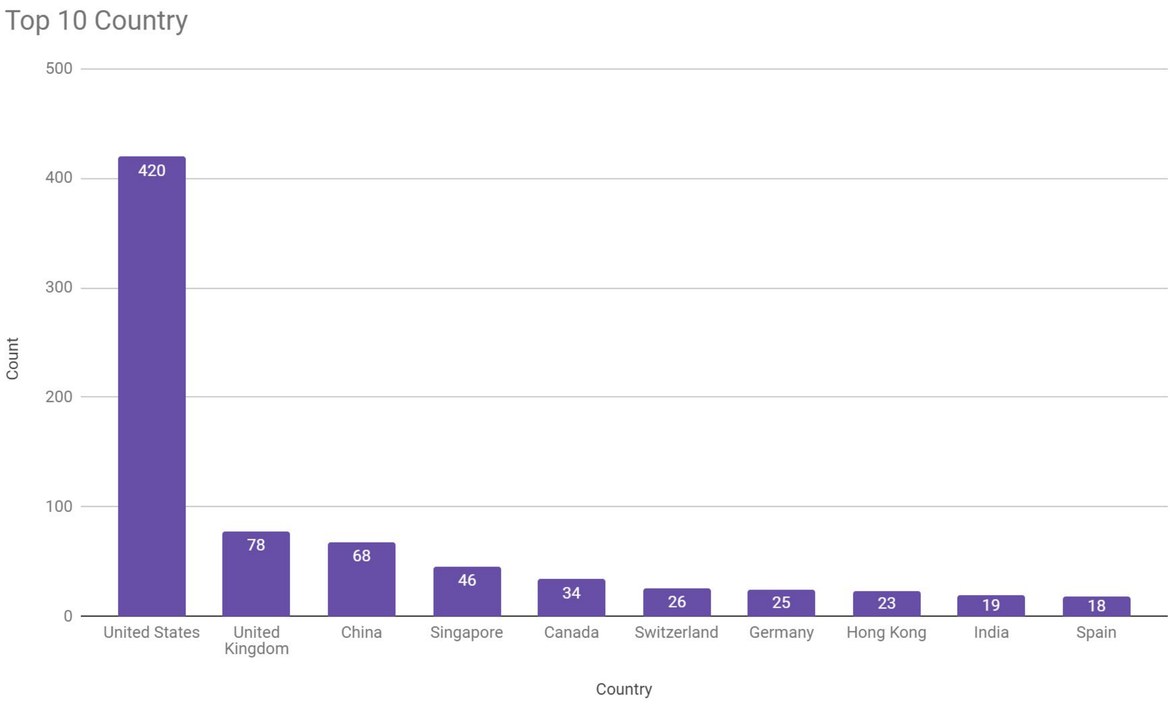
- **Chasing companies that are ill-prepared for follow on rounds**
  However, this frequency does not convert meaningfully to larger number of follow on-rounds. The mortality rate of blockchain companies are high due to challenges stemming from regulations, a lack of traction and access to investors that fund firms post series B

- **With misaligned incentives**
  The after effects of the ICO mania is becoming increasingly evident as startups struggle to optimally allocate capital raised or fine-tune themselves for growth. Easy capital with no expertise and quick returns add to the pressure founders have to optimise their companies for vanity metrics instead of focusing on long term growth.

- **And a lack of market expertise**
  The high number of rounds at early stages would mean institutional investors stick to investing increasingly on later stage firms with proven traction and product market fit. This leaves teams with the potential to be unicorns at the mercy of a handful of early stage financiers who bring nothing more than a cheque to the table.

Where you are headquartered matters

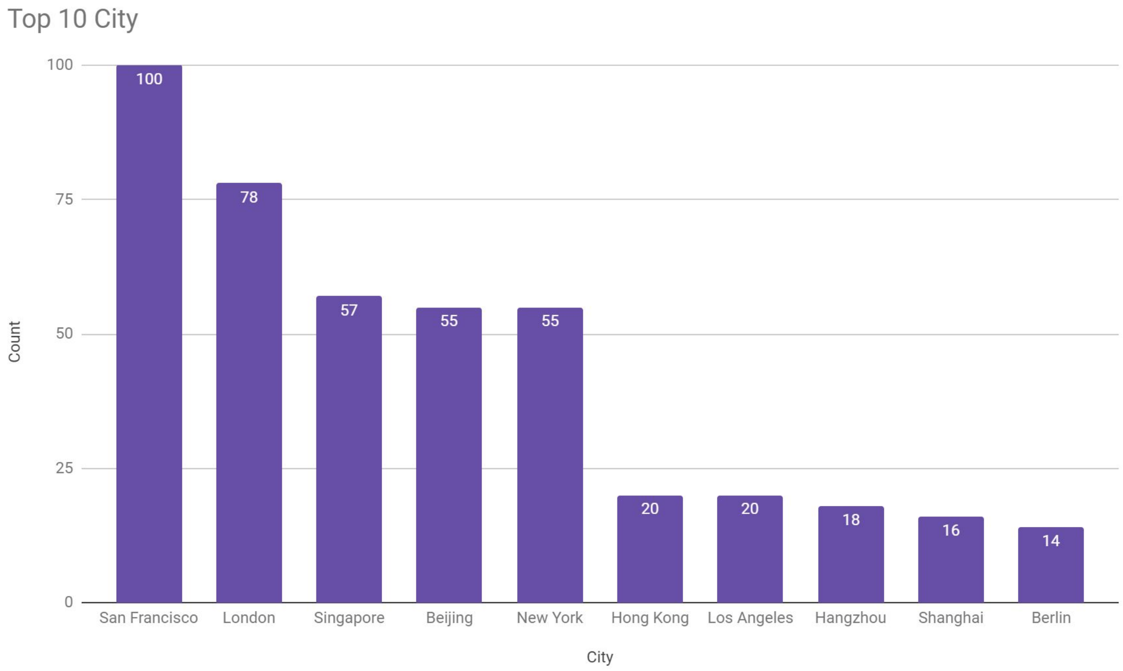
- The United States has more funded blockchain companies than the next 3 countries combined together.
- Investor appetite varies from region to region. Making free and fair competition impossible for what is fundamentally a global innovation



Note : Data specific to early stage financing for blockchain companies between 2017 and 2019. Source : Crunchbase

But cities are beginning to change the trend

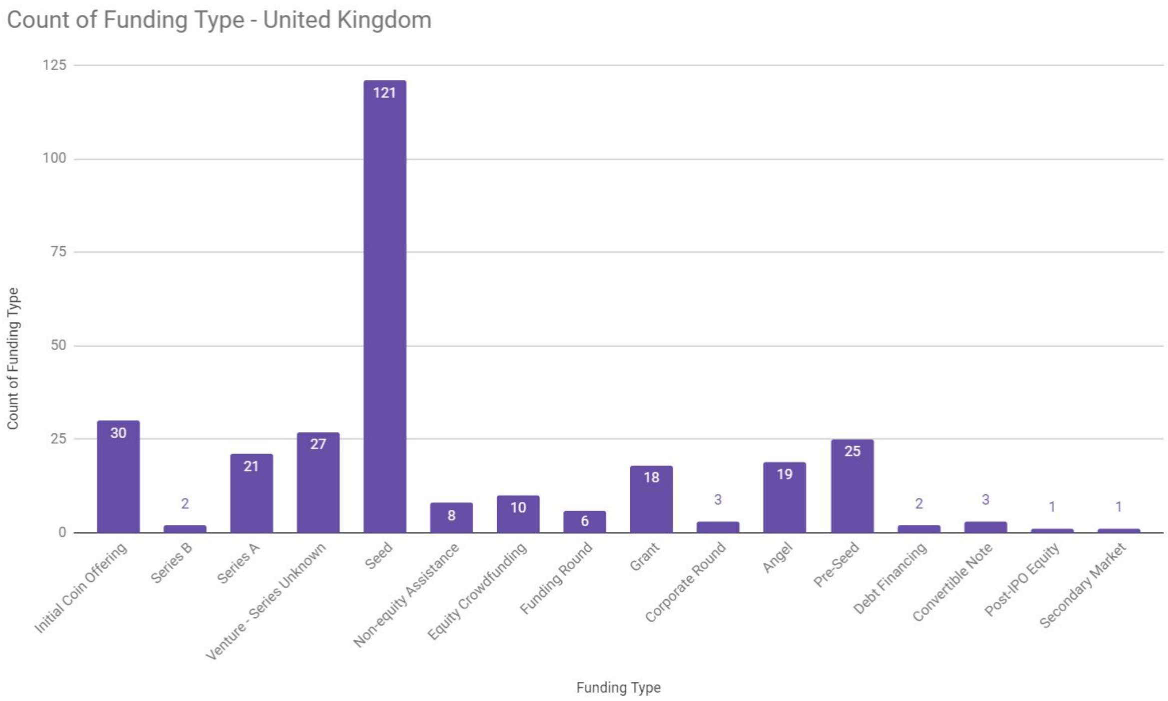
- When analysing at the city level - it becomes clear that Fintech hubs are a favourite for blockchain companies.
- San Francisco leads globally, but London trails closely. Regulatory changes may tip the scale in London's favor.
- Sandboxes set up in London and Singapore make them attractive for startups in Europe and South-East Asia to raise from.



Note : Data specific to early stage financing for blockchain companies between 2017 and 2019. Source : Crunchbase

London emerging as a hub for seed raises

- London has evolved to be a hub for early stage companies looking to raise seed stage rounds but the trend of few companies going on to raise Series A's and B's hold in the city.
- Only a fraction of companies in the region chose to go with ICOs in comparison to seed stage raises, indicating founder preference to raise institutional capital early on.
- Roughly $1 billion has been raised by companies in the region since 2013.



3 key takeaways

- Fundraising is cyclical
  Founders are dependent on Bitcoin's price to raise capital for what may not necessarily be a token dependent project. The heavy exposure of institutional players in the ecosystem to token prices swing risk appetites on basis of how tokens perform. This means heavy competition to raise from a handful of backers during bear markets, and heavy competition against a number of other equally well-funded projects during bull markets. Expertise and value added services are the only key differentiators that teams can rely upon

- Not all capital brings expertise
  The heavy competition in early stage financing for blockchain-based startups could mean a large number of investors bring nothing more than capital. Investments in equity are considered a hedge against liquid tokens. In addition to a lack of much needed guidance during the early stages, this also brings along expectations of quick exits from investors that are used to typically being in liquid assets like ICO tokens.

- Location matters
  Founder access to a network in regions where funding activity is heavy determines the possibility of the company going on to raise follow-on rounds. The United States leads globally when considered at a national level. Regional FinTech hubs such as London are catching up with former favorites such as San Francisco.

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To apply to be part of the program: https://outlierventures.io/base-camp/

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