

CYBER SECURITY VC FUNDING: IS THE BUBBLE ABOUT TO BURST?

ADDRESSING THE SILVER BULLET SYNDROME

By Katie Haug, Marketing Director

The cyber security industry boomed in 2017. Globally, cyber security investments ranked third in overall VC spending. According to Pitchbook*, VC firms invested \$7.6 billion in cyber security companies last year, up from \$3.8 billion in 2016. The number of cyber security-related investments jumped to 548 in 2017 from 467 deals the year before.

Average investments typically range from \$500,000 to \$5 million, however in 2017 investments were larger funds at faster rates.

As a result of the increased emphasis placed upon cyber security and strong growth of the market, Gartner predicted global cyber security spending to reach \$96.3 billion through 2018.

However, many experts believe this unprecedented boom is beginning to produce a 'silver bullet' syndrome with overvalued startups and a strong market correction on the horizon.



WHY THE BOOM?

2017 marked the largest amount of capital funding in history for the industry. The evolving technology ecosystem has become ripe for the taking as billions of funding dollars are at play.

Cyber security headlines rocked the news in 2017, including WannaCry and data breaches at Equifax and Uber. It was clear that VC firms took notice more than ever before.

VCs see potential to influence the competitive nature of startups they invest in, thus reaping clear financial benefits. In an interview with InfoSec Magazine, Venture Capitalist Nazo Moosa says, "Entrepreneurs often operate in the here-and-now, becoming very tactical and may need support to gain an overview of where markets are heading. Our ability is to sit above that and give a better view of the competitive landscape. It's about strategic focus, support of merger and acquisition activity, growing the contact base, helping to commercialize and scale their business."

THE VC PLAYERS

Investors are following the money and corporations and governments are increasing their spending on cyber security amid growing concern about vulnerabilities and breaches.

According to CIO Dive*, the four largest cyber security

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fundings in 2017 ranged from \$100 million to \$180 million, and NEA and Accel were the most active investors with nine deals each.

Most active investors in cyber security deals since 2013:

1. Accel
2. New Enterprise Associates
3. Bessemer Venture Partners, Intel Capital
4. Andreessen Horowitz, Sequoia Capital

While many venture firms reap great profit from these startups, there is potential downside and risk due to the growing number of startups to choose from. In an interview with CNBC, Rick Grinnell of Glasswing Ventures says, “One of the biggest threats to cyber investors is that their technologies may be proven to have holes or be exploited. If they are, their value essentially becomes negative.”

SILVER BULLET SYNDROME

Many experts believe a market correction is on the horizon in this overly crowded market. A large number of startups are now recognized as overvalued with potentially overpriced products.

In an interview with the Financial Times*, Norman Fiore, general partner at Dawn Capital, a venture capital group that is a keen investor in cyber security start-ups, says, “I don’t want to call it a bubble, but you did have valuations that ran away. You had lossmaking businesses growing fast but burning through lots of cash. There has been a move back to looking for companies with sound business models.”

Considering the year ahead, investors may be forced to painstakingly examine some of the more inexperienced cyber security startups before making projections about performance. There is a clear ‘silver bullet’ syndrome impacting the market and the best advice for VC firms is to avoid hype products at all costs.

Alberto Yopez, Founder of Trident Capital Cyber Security, the largest global capital firm focused on cyber, shares what he takes into consideration before investing (excerpt from an interview with Panda Security Mediacenter*):

“We look at five different areas — so this is a good note for entrepreneurs!

Number one, we’re really market driven. We like to get a sense of what the areas are where no commercial technologies exist so emerging solutions can be funded. So we look at, how big is the market?

Number two, we look at the intellectual property — how hard it is to replicate the solution.

Number three we look at the go-to-market strategy — how the company can scale not just by selling one at a time, but by creating alliances. Which is one of the basics to reach a global audience.

Number four we look at the team — whether the people have the experience, the context, the knowledge, and the relationships to be successful.

And number five, we often look at the co-investors. The investor group is important, because companies go through several iterations and several fund-raising, so you need investors that are committed to support a company through all this.”

*Sources:

Pitchbook; 2017 Year in Review: The top VC fundings & investors in cyber security.

Financial Times; Investors cool on cyber security start-ups that promise silver bullets.

Interview from Panda Security Mediacenter; Guest Collaboration with Alberto Yopez

CIO Dive; 2017; As VC investment booms, AI and cybersecurity startups rake in the big bucks