

Technology, Media & Telecommunications Practice

Europe's innovation wunderkinds: The rising B2B start-up ecosystem

While B2B start-ups are making Europe more competitive, start-ups, investors, and corporates will need to share expertise and work as partners to realize the region's full entrepreneurial potential.

by Karel Dörner, Tobias Henz, Max Flötotto, and Tobias Strålin

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Key insights

Three assets of the B2B landscape in Europe fuel its growth potential:

- *Great value for money:* European B2B start-ups¹ produce more output relative to their funding levels; revenue and valuations per invested dollar are higher than in the United States.
- *Mature regional ecosystem:* The key ingredients for success—talent, funding, and business partners—are available.
- *Fertile ground:* The European economy's need for innovation will likely further improve B2B start-ups' conditions for growth.

Calls to action for the ecosystem's key stakeholders:

- *Founders* should seize the opportunity from a quickly growing ecosystem and increasing investor interest to take ambitious steps forward.
- *Investors* should act on the potential to move more aggressively into the B2B start-up market yet provide their investments with the necessary expertise to increase the chance of success.
- *Corporates* should engage with start-ups across all phases to help both the start-ups and themselves.

¹ The term European start-ups refers to EU-based start-ups; UK-based start-ups have been excluded from this research.

Introduction

We definitely see an advantage for B2C start-ups in the United States, as investors and teams there are much bolder and relentlessly invest in growth. In B2B, however, European start-ups are excelling due to what we see as the region's technological advantage and the early value creation that comes from customer relationships.

—Hendrik Brandis, *Earlybird Venture Capital*

The European start-up landscape has for quite some time been best known for the success of B2C start-ups such as Deliveroo, FlixBus, and Revolut. In recent years, however, a handful of European B2B start-ups have achieved valuations of \$1 billion—and a few have even reached the coveted \$10 billion status—but mostly outside the public eye. Personio, sennder, UiPath, and Klarna (which is both B2B and B2C) are among the most notable, and several others B2B start-ups, such as KONUX and Forto, are well on their way.

This handful of current and soon-to-be European dynamos are just the most visible part of the strong and growing wave of high-performing B2B start-ups that are making the entrepreneurial scene in Europe much more competitive and attractive for investors. The B2B start-up space in Europe, in fact, might now be in a position to innovate on par with its peer in the United States.

To shed light on the rise of B2B start-ups in Europe and the implications of this growth on the overall start-up ecosystem in Europe, we conducted a course of quantitative and qualitative research (see sidebar, “About the research”). That research resulted in fresh insights into the success and potential of the European B2B start-up ecosystem.

About the research

The insights in this article were derived from quantitative analyses based on the following Crunchbase data set:

- more than 130,000 companies founded from 2010 to 2020 in Europe and the United States, out of which approximately 77,900 are B2B start-ups¹ and approximately 56,600 are B2C start-ups

- more than 85,000 recorded funding rounds, out of which approximately 70,000 specified the funding stage—for example, seed, series A, B, C, D, and later-stage

- more than 30,000 investors from all around the world who have actively been investing in start-ups founded between 2010 and 2020 in Europe and the United States

In addition, interviews with approximately 20 investors and founders of European B2B start-ups were conducted in January and February 2021.

¹ We classified the companies manually and based on specific keywords since the Crunchbase data do not contain such a characterization.

Success and potential of B2B start-ups in Europe

Three factors are likely to boost the growth potential of B2B start-ups in Europe: first, they provide great value for money; second, they profit from a mature regional ecosystem; and third, the European business landscape with its need for innovation is fertile ground for growing new innovation champions.

Great value for money: European B2B start-ups outperform their US-based peers in value per invested capital

We are seeing great value for money in the European B2B start-up landscape. That is why we have been establishing our fund.

—Alexander Kudlich, 468 Capital

The European start-up sector has long stood in the shadow of its US cousin.² For most of the last few decades, almost all of the world's major innovations have seemed to originate in the large venture clusters of Silicon Valley, San Francisco, New York, and Boston. In recent years, however, the European start-up ecosystem has given birth to major start-up successes that stand out in comparison with those in the United States. Among these are Swedish payment provider Klarna, which brought vast

innovation to e-commerce, and UiPath, a process-automation company launched in 2005 in Romania, now valued at more than \$10 billion. Other examples include the process-mining company Celonis, the HR-software company Personio, and digital freight-forwarding company sennder.

All these companies have achieved billion-dollar valuations, and many more European start-ups will likely follow suit. Beyond the most well-known examples, the broader B2B sector in Europe is experiencing very strong development and is now at least on pace with the B2B start-up sector in the United States.

Examining data on the past ten years in detail, we find that European B2B start-ups are outperforming their US counterparts in funding efficiency—that is, they generate more value (for example, revenue, external valuation) per invested capital. European B2B start-ups generate, on average, approximately 2.4 times the revenue per dollar invested compared with US-based B2B start-ups (Exhibit 1). The difference in revenue per invested capital is less pronounced for B2C start-ups but still significant: European start-ups generate about 1.2 times more revenue per dollar invested than their US counterparts.

2.4x

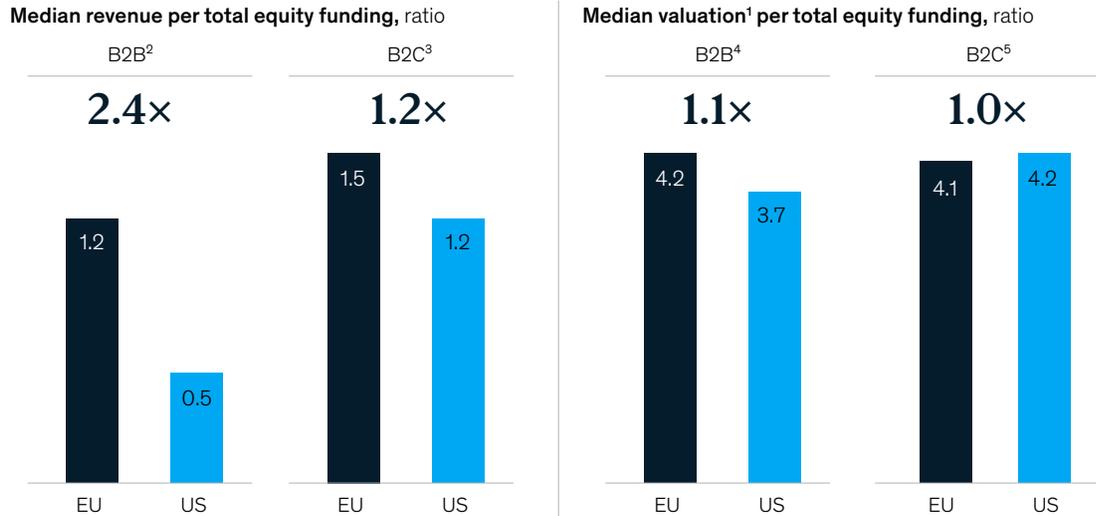
more revenue, on average, per \$1 invested generated by European B2B start-ups than US-based B2B start-ups

² Kim Baroudy, Jonatan Janmark, Abhi Satyavarapu, Tobias Strålin, and Zeno Ziemke, "Europe's start-up ecosystem: Heating up, but still facing challenges," October 11, 2020, McKinsey.com.

Exhibit 1

European B2B start-ups have better funding efficiency than their US and B2C counterparts, generating more value per invested capital.

All start-ups (B2B and B2C) founded 2010–20 in the EU and US



¹Valuations as published at funding rounds and recorded in Crunchbase database. ²EU, n = 4,127; US, n = 14,934. ³EU, n = 3,468; US, n = 8,891. ⁴EU, n = 508; US, n = 421. ⁵EU, n = 543; US, n = 301. Source: Crunchbase; McKinsey analysis

We observe a similar trend—though less pronounced—when examining the valuation-to-investment ratio: European B2B start-ups show an approximately 10 percent higher ratio compared with US-based B2B start-ups. Along this metric, European B2B start-ups also outperform European B2C start-ups.

There are several possible reasons for this disparity. First, European B2B founders came of age in an environment where capital was, at least until now, significantly less abundant than it was for their US counterparts. This reality likely engendered a more conservative expectation around fundraising, which might prove especially useful in regions without an established venture capital (VC) infrastructure and less of a tradition of private-sector investment in start-ups (Eastern Europe, for instance).

At the same time, the cost base in Europe is more favorable when it comes to several of the

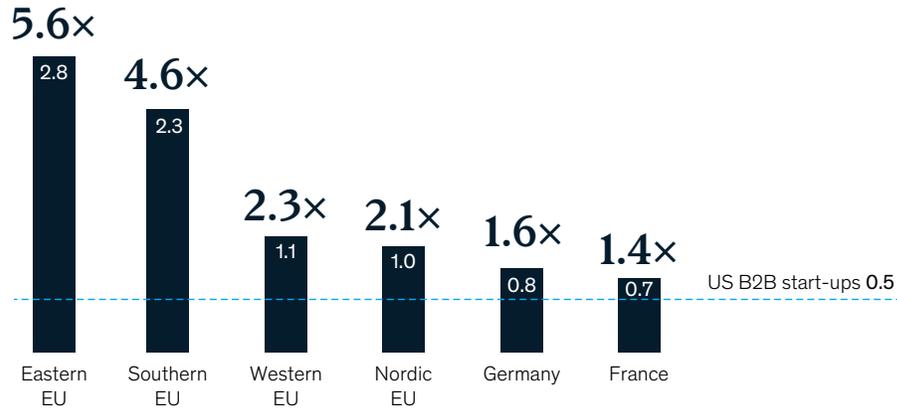
characteristics most relevant to start-ups. For example, several professional skill profiles critical to B2B start-ups (such as software developers) are often less costly in Europe than in many regions in the United States. Additionally, office rents in metropolitan locations in Europe are often lower compared with the start-up hot-spot regions in the United States.

Comparing different regions in Europe, we observe that the funding efficiency (revenue per total amount of funding) is indeed higher in regions in Eastern and Southern European countries, where funding is least abundant (Exhibit 2). By contrast, the largest European start-up ecosystems in Germany and France have the lowest revenue-per-funding ratios in Europe; nevertheless, they still generate about 1.5 times more revenue per dollar invested than B2B start-ups in the United States.

Exhibit 2

B2B start-ups in less developed parts of Europe boast higher capital efficiency than those in Germany or France, but all EU regions outdo the United States.

Median revenue per total equity funding, B2B start-ups, ratio



Source: Crunchbase; McKinsey analysis

When examining start-up growth potential in different sectors, Europe seems to have a great opportunity to develop a spike in industrial and technological applications, given the continent's strong industrial heritage. Capital efficiency is particularly pronounced in typical B2B tech industries such as aerospace, analytics, biotech, energy, enterprise software, and robotics. European start-ups in this space deliver more revenue per invested dollars than their US counterparts (Exhibit 3), and shifting priorities triggered by the COVID-19 pandemic could support their growth even further. In contrast, European start-ups in typical B2C industries (for example, e-commerce, food, social media) are delivering about the same value for funding as US-based B2C start-ups.

The European B2B start-up scene is growing significantly and, from an investor perspective, often providing great value for money given a stronger focus and mindset on capital efficiency and lower operating costs—for example, for software developers—than in the United States.
—Felix Haas, 10X Group

Mature regional ecosystem: The key ingredients for B2B start-ups' success are readily available in Europe

Back in 2015, the B2B start-up ecosystem in Europe was lacking experienced founders, investors, and corporate collaborators. Now this has changed, and we see the success with multiple multibillion-dollar companies.

—Alexander Kudlich, 468 Capital

Critical ingredients for the success of start-ups are becoming more obtainable in Europe, namely funding, talent and mindset, and an ecosystem of peers and partners.

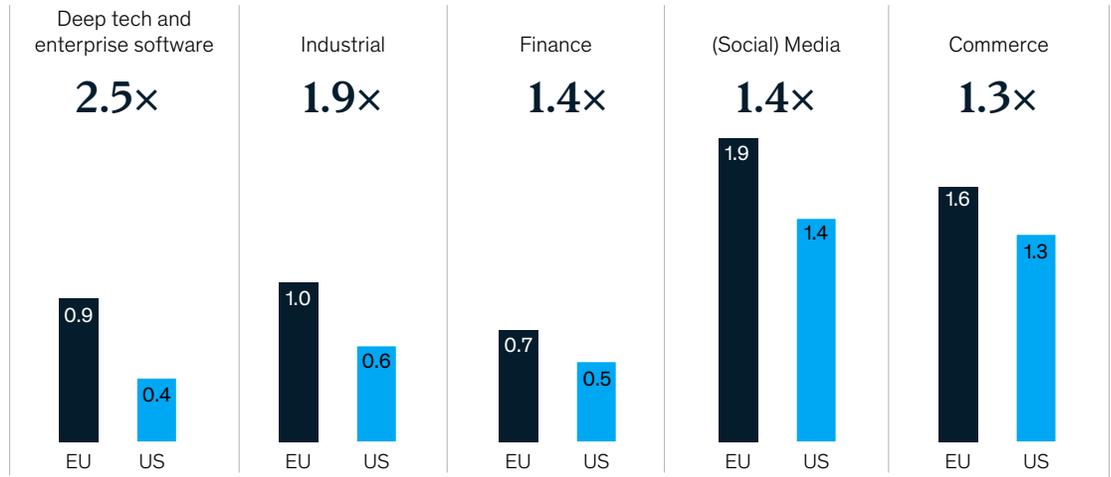
Funding

When we wanted to close a series A funding in 2016, we really struggled to find enough investors in Europe, particularly in Germany. This has now changed. For our series C round in January 2021, it has been relatively easy to raise money—although we were pretty selective in terms of the competencies we were looking for in new partners.
—Andreas Kunze, KONUX

Exhibit 3

EU start-ups in B2B domains outperform US peers in capital efficiency.

Median revenue per total equity funding, B2B start-ups, ratio



Source: Crunchbase; McKinsey analysis

Overall, start-ups have an easier time acquiring funding in the United States. That is particularly true in the B2B space, where the underlying technology and business models are often more complex than in the B2C space, requiring investors to bring more expertise to the table. The median equity funding for a B2B start-up in the United States is 2.7 times the median funding for a B2B start-up in Europe. For B2C start-ups, that factor is only 1.5.

However, drilling down and segmenting by growth stage, we see a different picture: the further along a European start-up is in fundraising, the more comparable the amount of funding it receives is to what its US counterparts raise (Exhibit 4). In the seed and series A funding rounds, US B2B start-ups raise about 1.6 to 1.7 times the funding of

European counterparts. By the time those same start-ups get to series C or later, however, that factor has decreased to 1.1.

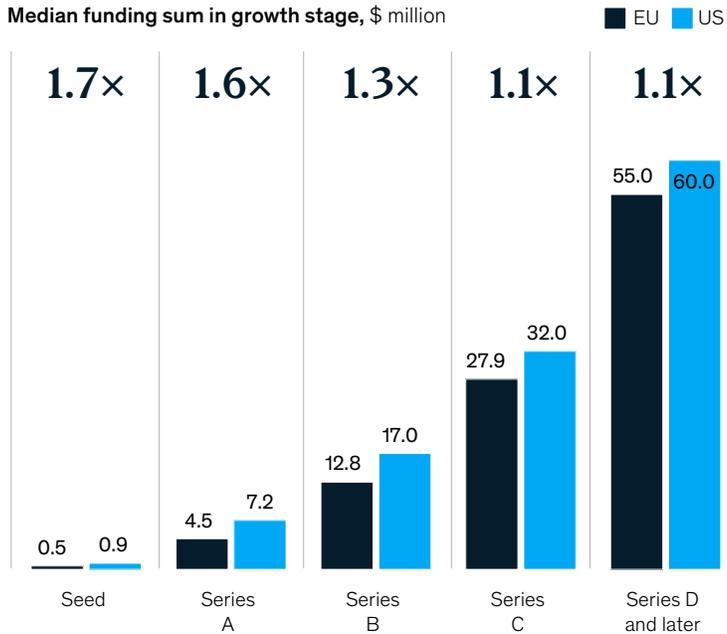
In the past five years, the number of growth-stage funding rounds for European B2B start-ups has grown by 123 percent and has not even decreased during the COVID-19 crisis. Prominent examples of larger growth-stage funding rounds during the crisis include the railway-software platform KONUX, the Berlin-based vertical-farming player Infarm, and the previously mentioned Personio. By contrast, in the United States, this number has only grown by 40 percent. That gap hardly exists for B2C start-up investments, with European growth-stage funding rounds up by 28 percent, compared with 22 percent for the United States.

Exhibit 4

Funding of EU B2B start-ups trails that of US peers early on, but the gap is narrowed in later stages.

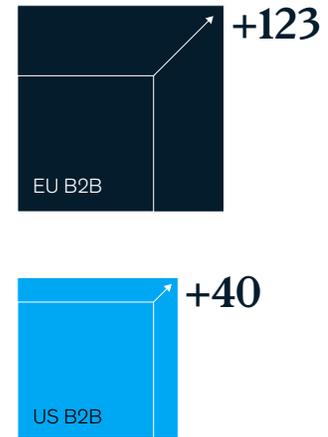
European B2B start-ups raise similar amounts in later rounds ...

Median funding sum in growth stage, \$ million



... and the total number of rounds in the EU is growing faster than in the US

Increase in number of series A–C funding rounds, 2015–20, %



Source: Crunchbase; McKinsey analysis

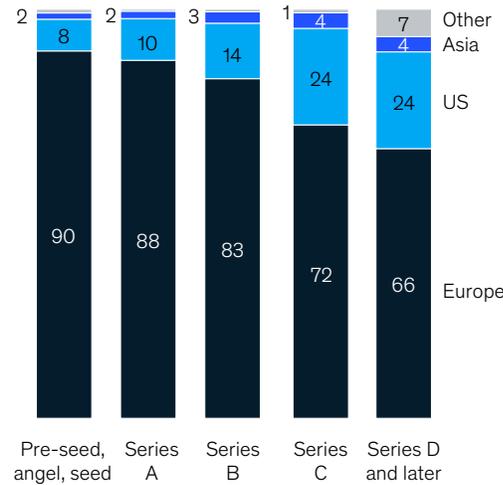
This funding dynamic is fueled by both sides of the Atlantic. On the one hand, US investors are extremely interested in funding the growth stage (series C and later) of European B2B start-ups, accounting for almost a quarter of the total number of investors (Exhibit 5). But their interest in early-stage start-ups is also increasing: the share of US investors in European B2B seed-funding rounds has increased by 78 percent over the past five years. Recent examples of US investments in the seed stage of European start-ups include the German productivity player Layer, Finnish vertical-farming tech start-up iFarm, and the Portuguese fintech company Balancer Labs.

On the other hand, the European investment ecosystem itself is maturing. Along with the rise of specialized B2B investment funds and the inflow of growth-stage VC money, corporate investors are stepping up their game of investing in growth-stage start-ups. For example, last year, corporate VC investors participated in more than 210 percent more funding rounds (series A–C) than in 2015 (Exhibit 6). Another positive sign for the maturing investment ecosystem is the increasing number of B2B growth-stage rounds that included the participation of angel investors who are also cofounders in relatively new start-ups (225 percent increase during the past five years).

Exhibit 5

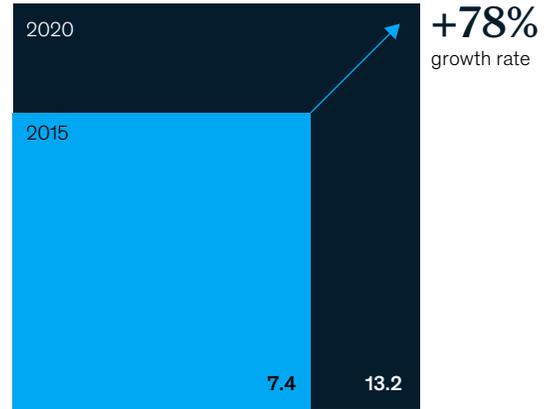
Almost a quarter of growth-stage funding for EU B2B start-ups comes from US investors, who are also increasingly contributing to seed funding.

Share of investors in funding rounds by country of origin, %



Note: Figures may not sum to 100%, because of rounding.
Source: Crunchbase; McKinsey analysis

Share of US-based investors in EU B2B seed rounds, %



One gap that remains to be closed, however, is the level of professionalization that established US investors typically bring to the table. While European investors are beginning to make more significant capital investments, they don't yet have the decades of experience that would allow them also to share equally valuable tools, expertise, and best practices with start-ups.

Much more than the money invested, we largely benefited from the capabilities offered by our US investors along the value chain. The tool set we received from them and their help in professionalizing processes from recruiting to sales has been invaluable. And most European players do not just yet have the resources to offer something similar.

—André Christ, *LeanIX*

Talent

Along with the ability to acquire funding, talent is an equally important factor for the success of a venture. In contrast to many B2C areas, B2B often requires specific business expertise and, for many domains, a deep technological understanding. Several characteristics have made Europe an excellent source of such talent:

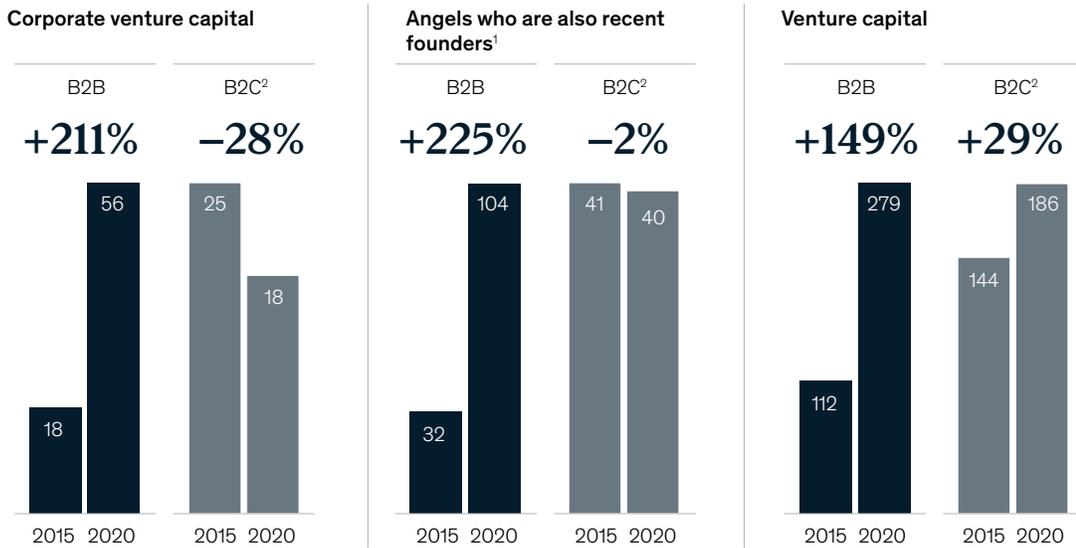
- **Top-tier institutions.** Europe has a high density of top-flight educational institutions, putting its research base on an equally vaunted level with that of the United States.³ The challenge will be to cultivate a start-up environment in Europe that is as attractive to young talent—in creativity, opportunity, innovation, and compensation—as it is in the alluring start-up meccas of the United States.

³ Philipp Ernst, Matthias Evers, Ivan Ostojic, and Sebastian Stern, "How growth can help Europe's companies face the coming economic crisis," May 13, 2020, McKinsey.com.

Exhibit 6

The growth in funding rounds for EU B2B start-ups is driven by an expanding and maturing European investment ecosystem.

Series A–C funding rounds for EU start-ups by investor type, 2015–20, number



¹Number of rounds that included the participation of angel investors who were also cofounders of other start-ups that were founded between 2010 and 2020.

²For 2020, the COVID-19 crisis is expected to have a more significant negative effect on investments in B2C than B2B start-ups. However, the effect is stable when comparing 2015 with 2019.

Source: Crunchbase; McKinsey analysis

211%

rise in corporate venture-capital-investor participation in Series A–C funding rounds for EU B2B start-ups between 2015 and 2020

- **Deep industry expertise.** As the business culture in Europe shifts away from a singular focus on incumbent companies in traditional industries toward an appreciation for entrepreneurship, many “corporate type” professionals are now looking for ways to get involved in the start-up scene. These experts’ willingness to lend their knowledge and deep industry expertise is a significant resource for start-ups as they navigate the corporate environment.
- **Bold entrepreneurial spirit.** European founders are increasingly characterized by a “think big” approach to entrepreneurship. This approach is evidenced by more and more early expansions beyond their borders (across Europe and even into the United States). Examples include Delivery Hero’s rapid global expansion, sender’s highly successful move into Italy, and LeanIX’s presence in the US market.
- **Founders’ legacy.** The European start-up ecosystem has matured to yield a significant group of successful serial entrepreneurs, with 8.3 percent of recent B2B founders in Europe having founded at least one other venture.

While this still lags behind the United States (11.5 percent), the gap is closing. This reality results in two specific assets moving forward: these founders are now bringing deep experience from past ventures into their own new B2B businesses, and they are also in a good position to nurture the B2B start-up ecosystem by mentoring and supporting other founders.

Ecosystem partners

With its historically strong industrial and manufacturing sector, Germany offers not only a broad platform of potential customers for many B2B topics but also a great opportunity to establish reference cases as a springboard for internationalizing the offering.

—Andreas Kunze, KONUX

Partnering with established companies is incredibly important for B2B start-ups. Incumbents not only are natural customers but also can be essential in helping to develop a product toward the optimal market fit. In the process, they can make it easier to find a critical mass of customers, or they could possibly even end up acquiring the venture.

Along with the ability to acquire funding, talent is an equally important factor for the success of a venture—B2B often requires specific business expertise and a deep technological understanding.

A survey among start-ups from the DACH region (comprising the majority German-speaking countries of Germany, Austria, and Switzerland) has shown that B2B start-ups are especially interested in such partnerships and that they look for more than just the revenue boosts that accompany them.⁴ This rising enthusiasm is now being reciprocated on the corporate side, where a new generation of top management that understands the potential benefits of innovation for themselves seems more open to collaborating with start-ups.

The spirit of collaboration observable in US corporates is beginning to have a positive impact on the B2B start-up ecosystem in Europe. As more US tech companies open local offices and R&D centers in the region, the opportunities for EU B2B start-ups to collaborate or be acquired are growing.⁵

Finally, as some European start-ups scale and mature, they become the type of resource to younger start-ups that their own corporate partners had been to them. One example is European e-commerce company Zalando. Beyond its product offerings in fashion and housewares to consumers, the 12-year-old company is now a platform that offers marketplace solutions for younger B2B start-ups.

Fertile ground: The need for innovation in Europe's economy will further improve B2B start-ups' conditions for growing into innovation champions

The European economy is in deep need of innovation. Given Europe's relatively high wage structure and low reliance on natural resources, innovation remains of fundamental importance to the continent's economic and social futures. Yet the share of European companies that consider themselves true innovators is notably lower than in the United States.⁶

Disruptive technologies and new ways of working can be part of a transformation that helps Europe to strengthen its market position in an increasingly competitive global marketplace. The COVID-19 crisis has only added to this pressure to improve and reinvent how business is conducted. Start-ups are key in bringing innovation and its accompanying competitive advantage to all industries—from finance to deep tech. B2B start-ups in Europe could significantly uplift the modernizing of the European economy by partnering with and selling their products to established companies.

Beyond partnering and selling to established companies, B2B start-ups in Europe will also contribute to a new European economy just by growing in size themselves.

Unlike the B2C space in Europe—where start-ups must navigate different cultures of the different countries and their distinct consumer markets—the landscape of business customers is more homogeneous. Businesses across the continent still tend to follow more predictable and similar rules. Hence, a venture can be grown regionally or even globally more easily without having to spend so much time and resources adapting the product to specific local markets.

Harnessing the opportunities of the European B2B start-up ecosystem: A call to action

While funding opportunities have increased, it is still the case that European B2B start-ups obtain fewer funding rounds than their US counterparts (an average of 1.9 versus 2.5 for US peers), and only 27 percent of European B2B start-ups advance from seed to series A compared with 46 percent of their US peers (Exhibit 7).

⁴ Karel Dörner, Max Flötotto, Tobias Henz, and Tobias Strálin, "Can't buy love: Corporate-start-up partnerships in the DACH region," September 30, 2020, McKinsey.com.

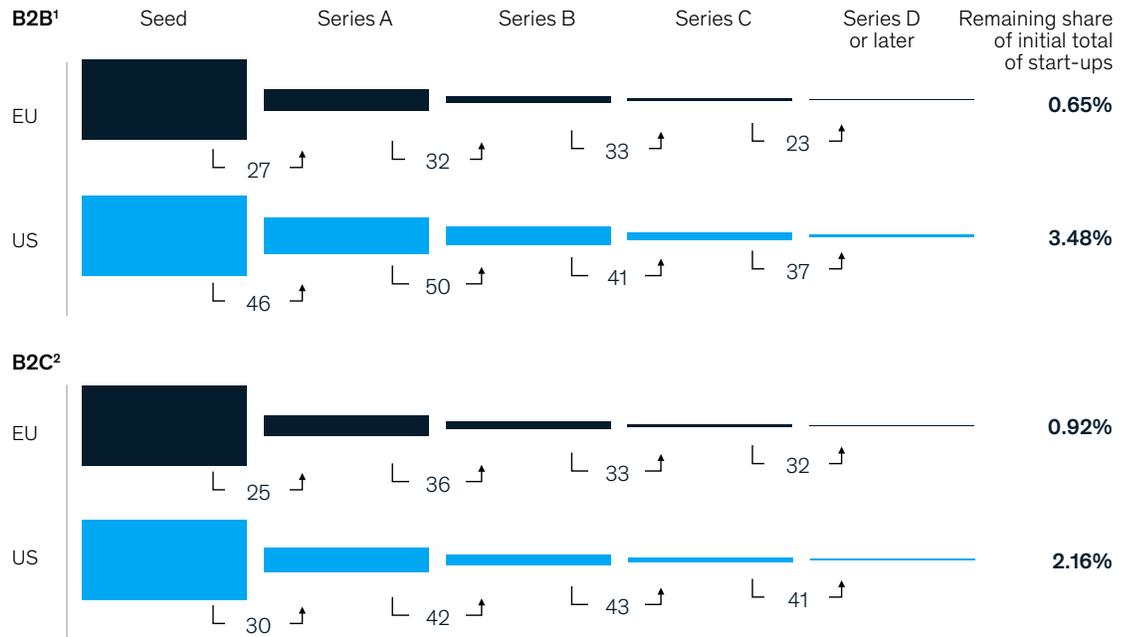
⁵ Maija Palmer, "Why do European companies buy so few startups?," Sifted, August 11, 2020, sifted.eu.

⁶ See Jacques Bughin, Bernhard Gürich, Jan Mischke, Pal Erik Sjatil, Sven Smit, and Eckart Windhagen, "Reviving innovation in Europe," McKinsey Global Institute, October 16, 2019, McKinsey.com.

Exhibit 7

EU B2B start-ups fail earlier and more frequently than their US peers, while the difference in B2C success rates is much less pronounced.

Share of start-ups founded between 2010–15 reaching the next funding stage, %



¹EU, n = ~3,850; US, n = ~10,650. ²EU, n = ~3,900; US, n = ~8,300. Source: Crunchbase; McKinsey analysis

The timing of funding also plays a central role in start-up success. Not only do European-based start-ups get fewer funding rounds, but it also takes them longer to get there—on average, half a year longer to raise a series A or B than US B2B start-ups. Long corporate-decision timelines and rigid budget processes are some of the reasons for this gap, but there are clear commitments that the start-ups themselves, their investors, and established companies in the space can make to move the entire European ecosystem forward.

Start-ups and founders: Complement your strengths with investors’ and corporates’ expertise

The rising amount of growth-stage funding rounds is a good sign for the fast-developing European B2B start-up scene. This trend should encourage founders to stay ambitious and focus on scaling their companies. Meanwhile, the growing share

of US investments is also sending a strong signal and comes with practical advantages for start-ups. As more US investors enter the market, European founders will not only have better access to growth-stage funding but also can leverage US investors to enter the US market earlier.

Attention is growing from not only foreign investors but also European corporates that need to boost innovation and are finally opening up to investing in or partnering with start-ups. That means that B2B start-ups and their founders do not necessarily have to move into attractive but expensive and crowded start-up hubs such as the United States to be closer to promising markets. Instead, they can leverage the higher efficiency and unchallenged access to talent in their home markets while being able to scale together with European corporates.

Investors: Leverage your expertise

Europe is a clear winner when it comes to value-for-money investments. That is especially true in B2B, where start-ups show great resource efficiency and technological know-how and the market is not yet overrun by investors competing for the same deals. The increased attention from US investors is overall a positive trend for all investors, as the influx of capital increases the value of the target start-ups.

With that being said, the law of diminishing returns applies here. Some foreign investment is an asset for potential European investors, but if it accelerates while the majority of European investors remain on the sidelines, the funding opportunities for them will be harder to come by. More European investors need to commit to growth-stage funding to be able to maintain the upward trend of catching up with (or even overtaking) their US counterparts.

Yet investments should mean more than an injection of capital. Especially in the B2B sector, deep expertise from investors is necessary to support the ventures' growth. Hence, investors should focus on a few selected domains and expand their teams with suitable experts.

To substantially grow this sector and become competitive with the United States, we need four to five large funds in Europe that are able to raise more than \$1 billion. We need the capacity to fund a \$100 million series B round.

—Hendrik Brandis, *Earlybird Venture Capital*

Corporates: Develop start-ups as true partners

The European B2B sector is thriving and innovating at great speed, which comes with

a huge opportunity for European corporates. However, to realize the potential benefits, established companies in Europe will need to move more boldly into the start-up landscape. Many US tech titans have shown that these strategies can be highly successful, incorporating a significant number of start-ups over time—some of which have contributed core products to the product portfolio.

There is a great opportunity for corporates to support start-ups from the beginning, shape the products to their needs through codevelopment, and thus create innovation pipelines that do not require building an expensive corporate VC infrastructure. Getting there, however, requires corporate top management to be less hesitant about partnering with start-ups in the first place.

Europe is beginning to stake a sizable claim in the start-up world. While it is the VC and innovation centers in the United States that still dominate in the B2C sphere, Europe's B2B start-up ecosystem has unique strengths that could set the stage for the type of success that is defined not only by revenue at the individual level but also by innovation that benefits the entire regional economy. To realize this potential, however, both corporates and investors in the region need to understand the mutual interest in the success of Europe's B2B ecosystem and partner with and invest in start-ups to make that a reality.

Karel Dörner and **Max Flötotto** are senior partners in McKinsey's Munich office, where **Tobias Henz** is an associate partner; **Tobias Strålin** is a partner in the Stockholm office.

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