Will the world ever see a 'water' unicorn?

Unicorns, (new companies valued at $1 billion or higher) were so named because of their rarity. While certain industries, such as finance and software have each generated 200+ unicorns to date, a water industry unicorn has yet to emerge.

We asked leading investors: Will the world ever see a 'water' unicorn?

Meet the Experts

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There will be no water unicorns – at least in the traditional '10x' sense.

The water industry and its incumbents (water-focused Fortune 500 companies, OEMs, service companies, general contractors, municipalities, etc.) are deliberate and conservative. Not because they are lazy, overly administrative in nature, or because they 'don't get it', but because they serve and master the most important and delicate sector in our global system. Conservative decision-making is the standard because disrupting the processes and systems that reliably provide clean water is a sensitive endeavor – even if supported by the best of intentions.

Water investing is still in its adolescence, and so far, it has, narrowly and wrongly, been defined mostly as 'water technology' investment. As a result, the first wave of venture capital investment firms 'hit the ground running' by pouring (pun intended) capital into early-stage water tech companies – most of which failed.

In addition to the typical hype and 'over-reaching' (and under-thinking) when investing into new investment categories and asset classes (Think: dotcom, renewable energy, blockchain, cannabis, anything-as-a-service, etc.), we must be aware of the 'returns reality'. The 5 to 10x investment multiple does not exist in the water industry as a repeatable event. This is because neither the incumbents nor the (very few) financial investors are incentivized, nor have the money, to overpay for 'up-and-coming' water technologies or business models.

This conclusion rules out the traditional venture capital investment model as a viable investment approach in water (and with it, the hunt for unicorns), since venture capital portfolio management relies on one or several high multiple exits to make up for the losses expected in a risky portfolio of this kind. In other words, the overall risk-return profile of the water industry deals a lopsided hand – in the wrong direction – to venture capitalists.

So, what type of investment and finance model works given the water industry's pressing need to renew itself and improve its chances against population growth, aging infrastructure, and tightening regulatory requirements?

In my view, the growth equity and private equity investment model seems more suitable. The private equity model – especially the 'hands-on' version of it – aims to invest in business models and true commercial value propositions rather than technologies.

It reviews investment opportunities across the entire value chain of water – not just technology investments – and it is more conservative (more risk-averse). It aims for investments with risk-return profiles investment structures that consistently returns its entire capital investment, and in most cases receive a 2-4x investment multiple over 3-6 years. Therefore, the private equity investment approach suits the water industry well because the return expectations are more aligned with the sector's traditional growth patterns and are also more representative of the exit multiples currently available in the industry.

In my view, the water industry is similar to most other commodity-based industries with an upstream, midstream, downstream and service component – but with steadily increasing water prices allowing for investment opportunities across this value chain. The unhurried, calculated, and traditional cycles of the water sectors are fairly set despite a dire need for the industry to reinvent itself. Successful water investing requires subject matter expertise, appropriate financial partners and models, and realistic prospects. If executed correctly, a level-headed investor will be able to yield from this 'slow moving tsunami' of investment opportunities in the water economy for years and years to come.

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> *- Brian Iversen*

Fredrik Östbye

CEO, Aliaxis Next

Unicorns are created by entrepreneurs. When something is perceived as a free, and endless resource, it doesn't attract entrepreneurs. But both the perception and the reality of water as a free and endless resource is changing.

Humanity is realizing that if we continue using our most precious resource the way we do, we will run out of it in big areas of the world, already within a decade. Half the population is predicted to live in water stressed areas by 2030.

If you are running out of something, you either must reduce consumption, add more, or do both. Tech can do this, and entrepreneurs love to use tech to build new businesses, and we see lots of new companies around the world are being built to manage water in more sustainable ways.

In agriculture, using 70% of the freshwater withdrawal, we see solutions reducing need of water for irrigation in outdoor farming with 30%.

New ways of growing crops in controlled environments like greenhouses, containers, and vertical farms, reducing need of water with 95%. And new ways of growing proteins, reducing need of water with 90%.

In industrial processes, using 20% of the freshwater withdrawal, we see solutions reducing and reusing water, but also completely taking out the need for water in water intense processes.

In buildings and municipalities, using remaining 10%, we see solutions reducing and reusing water, but also solutions to build smarter and more resilient infrastructures to transport water.

And solutions to capture and manage rain- and stormwater, turning it into an asset instead of a problem.

Water is also a carrier of manmade forever chemicals (PFAS), ending up in our bodies through the water we drink and the food we eat, with big health risks as result. New solutions to take out PFAS are emerging and may become a big thing.

An interesting exercise to do is to imagine yourself sitting on the moon, looking down at planet Earth. Then you most likely will think that water can never be an issue, as 70% of the planet is covered of it. New solutions to add more freshwater into the equation are also emerging, within desalination and atmospheric water.

New, fast-growing companies will also emerge, bringing water to the 1.4billion people who have money to buy safely managed water, but no reliable infrastructure bringing it to their homes. And solutions to the 800 million people with no, or limited, financial means, who today are using untreated water straight from nature.

Most of these emerging companies are using digital tech, and they are going for exponential growth, enabled by recurring business models, digital marketing, and full focus on customer experience, why I am 100% convinced that we will see the first `water´ unicorns emerge within the next decade. I can see them growing up out there already.

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John Robinson

Partner,
Mazarine Ventures

The world will never see a ‘water’ unicorn.

What we will see is a company that achieves unicorn status by leveraging technology to help its customers address water-related risks.

Unicorns like Planet Labs (earth observation tech) and soon-to-be unicorn Tomorrow.io (weather tech) would never describe themselves using terms like ‘water company’ or ‘water industry’ but their tools are helping their customers manage water-related risks, which span customers in agriculture, aquaculture, finance, insurance, real estate, mineral processing, manufacturing, utilities, and public health and safety.

Examples from the Mazarine portfolio include software company SimpleLab, which helps their customers manage water-quality risks, and Agcor, a finance company that is helping their customers manage quantity risks. Neither would ever say they are in ‘the water industry, as you frame it.

Is Liquid Death, a ‘water unicorn’?

As Blackrock CEO, Larry Fink, so famously said, the next 1,000 billion-dollar startups (unicorns) will be in ClimateTech, which will include companies that help industry and society manage climate-change-induced water risks.

A company that can bring to market Point of Use filtration with an app that tells you if the filter media is working could become a unicorn, but we filter our water at home for family health, making that company a 'health-tech' unicorn, not a so-called ‘water’ unicorn.

That's why there will never be a ‘water’ unicorn.

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- John Robinson

Ginger Rothrock

Senior Director,
HG Ventures

Venture capital models have historically focused on digital businesses with predictable growth trajectories, time to market, and capital need. “Hardtech” startups don’t fit this playbook and fewer venture funds have invested in this category. Limited partners (LPs) perceive hardtech to be high-risk and question their capacity to source and diligence these investments. As expected, therefore, industries rich with investment capital have thrived and produced unicorns.

The climate crisis has resulted in innovation, attention, and investment in the environmental hardtech sector. Yet the action is concentrated on carbon. Water, the other essential global cycle, remains invisible. Water has been an inexpensive, low volatility, consistent utility. However, recent events including the overtapped Colorado river, lake levels, and California flooding have accentuated the necessity of water security and management.

The industrial sector consumes up to 40% of the world’s water supply, yielding extensive exposure to resource risk. Water is (pun intended) a blue ocean for industrial innovation that solves supply chain risk and corporate resiliency, creating the environment for a water unicorn. For example, industrial wastewater processing hasn’t substantially changed in over a century: facilities pay to haul contaminated water offsite or hire technicians to perform time-intensive manual testing and treatment.

I predict the combination of economic impact, public pressure, and technology innovation will drive multiple water companies to unicorn status within 5-7 years. Labor shortages and supply chain pressures have led businesses to accelerate automation technologies like robots and smarter software combined with hardware that is more powerful, user friendly and affordable. Emerging automated, onsite solutions monitor and treat contamination, enabling compliant discharge and economical recycling of industrial water.

For example, Electramet removes heavy metals from wastewater using an automated membrane-free and chemical-free process. ZwitterCo is deploying fouling-resistant membranes that treat challenging organic streams, focusing on product purification and chemical reuse.

The digital transition continues to permeate legacy industries, and digital water products have material unicorn potential. Assets and reporting compliance is largely digitized, with water quality monitoring and waste at a nascent stage.

Design automation is emerging in public and private sectors; asset owners want to understand and weigh options in risk, carbon footprint, and cost before they build facilities.

One company, Transcend, offers software that automates the engineering design process for water treatment facilities.

Investments in the water sector are becoming more attractive as the business models adapt. Rather than large scale, CapEx-intensive facilities, industrial water monitoring and treatment innovations are moving towards decentralized automated units.Pricing models include leasing and software monitoring in a recurring fee, mimicking the high margin “as-a-service” models traditionally found in the tech industry. Customers value the reduced workforce needs, exchange of CapEx and irregular supply purchases to a predictable operational expense, and measurable sustainability benefits.

It takes industry expertise and collaboration to build these nascent opportunities in water to unicorn status. Market trends in sustainability, economics, and regulations all signal coming industry-disruptive growth for water startups that detect and remove contaminants, provide circular solutions for value, and yield efficiencies for industrial companies.

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