

Venture Capitalism in the Mental Healthcare Sector after the COVID-19 Pandemic

By Eddie Wang

AUTHOR BIO

Eddie Wang is currently a student in Houston, Texas. He was born in China and has studied in the UK during primary school as well as in an international school in Beijing during middle school. He is part of his school's speech and debate team, Model UN team, and has competed in math competitions such as the AMC 10 and as part of the academic team. His personal interests include studying chemistry, world history, and playing the piano. In his spare time he enjoys reading, writing, and challenging his friends to a game of table tennis.

ABSTRACT

The COVID-19 pandemic was to date the largest-scale disease outbreak of the 21st century. It has had far-reaching consequences in all aspects of life. One of the most significant is the global increase in the prevalence of mental health concerns, in turn placing mental healthcare companies front and center for demand. Investors, deprived of many industries which did not escape the financial crisis brought on by the pandemic, may view the emerging mental health sector as an auspicious target. This paper analyzes the impact of COVID-19 on venture capitalism in the mental healthcare sector through comparisons of pre- and post-pandemic states of the financial market and use of case studies of various companies involved in mental health. A generally positive correlation can be seen between the outbreak of the virus and growth in investment. Using these findings, this paper suggests directions for venture capital investment, such as in startups, which balance out potential profit and risk.

Keywords: *COVID-19, Mental health, Investment, Venture Capital, Startup Company.*

INTRODUCTION

When COVID-19 hit in early 2020, the world was caught unprepared. Since its onset, it has caused the death of nearly 7 million people¹ and severe economic recessions. Despite being responsible for the near-collapse of many industries, COVID-19 has inadvertently led to the rise of other markets, most notably mental healthcare. Heavy restrictions and lockdowns implemented to combat the pandemic transformed the lives of billions of people, forcing them to adapt to a post-pandemic lifestyle including remote work and reduction in social activity. Many had to deal with the trauma of losing family members, rising unemployment and extended periods of isolation.

These dramatic changes caused widespread mental distress, increasing global anxiety and depression rates by 25%.² In the US, where the virus was particularly prevalent, around 40% of adults reported symptoms of anxiety or depression in 2021, up from just 10% in 2019.³ Such a dramatic upsurge in psychiatric issues furthered demand for mental health services on a scale unparalleled in history. The impact of the COVID-19 pandemic on mental health created the perfect condition for a greater market for mental health service providers.

Opportunities for Investment in Mental Health

In 2021, the global mental health market was valued at \$401.31 billion and is expected to reach \$551 billion by 2030, growing at a compound annual rate of 3.5%.⁴ The fastest expanding sector was mental health apps with a market size of \$4.2 billion, up by 54.6% from 2019.⁵ This growth has been catalyzed by COVID-19, as limitations on travel forced the majority of services to move from in-person to online. As many as 96% of mental health services were digitally provided during the

pandemic.⁶ New startups have been quick to capitalize on this trend and use digital resources like apps to ensure broader access to customers.

The startup market for mental healthcare has opened up lucrative opportunities for venture capitalists. Many of the mental health app developers, encouraged by their success so far in the industry, are initiating new rounds of funding to improve their services. The unprecedented growth rate of the mental health app market is a safe bet to yield high return on VC investments.

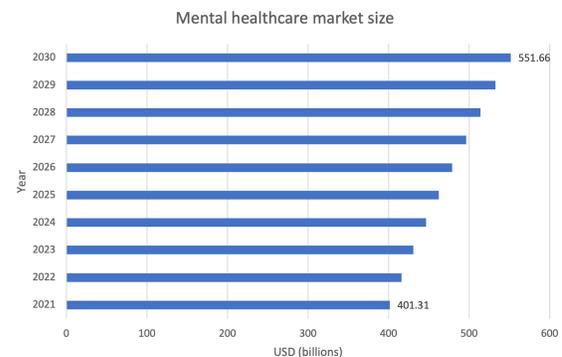


Figure 1. Projected mental healthcare market size between 2021 and 2030 (Source: Emergen Research)

Case study: Real

The startup Real recently raised \$37 million in series B investment led by Owl Ventures after completing \$10 million in their series A round last year.⁷ Real, founded in 2019 by CEO Ariela Safira, provides on-demand group therapies through its online platform. It seeks to expand the accessibility of mental healthcare while simultaneously reducing its cost. Among its key features are “pathways” consisting of multiple sessions and exercises which address specific health issues.⁸

“We’re redesigning mental health care through a digital platform and in-person experiences, integrating empathy, design, and progressive care to build the most elevated

end-to-end product, while also improving the quality of care itself,” Safira outlined as the company’s goal.

Due to its focus on digital services, Real hit the jackpot during the pandemic, which all but halted traditional service providers. Real was thus able to pioneer the new age of mental healthcare, with its services being sophisticated and satisfactory to the public. Its digital foundation also allowed it to adapt almost seamlessly to COVID-19, as seen when it replaced its planned in-person studio in New York with a new therapy website in early 2020 within just 8 days. Real has since become one of the fastest-developing mental health ventures, rising in the market with a total valuation of \$53 million.

In cases like Real, venture capital investment would be more profitable when conducted sooner rather than later. Investing when the startup is at a relatively early stage ensures a lower pre-money valuation before the funding round, allowing a lower valuation cap to be negotiated. This increases the percent ownership of the company acquired through the funding, boosting conversion into equity in the event of liquidation or into stocks if the company undergoes an Initial Public Offering. A higher percent ownership also translates into more influence on the startup’s management, such as having more places in the board of directors. All of these are beneficial to VC investors who aim to extract the maximum revenue from their investment and orient the company in the right direction to achieve this.

This highlights the importance of timeliness in investing. Done too early, and the risk outweighs the return. Done too late, and the return drops considerably. It is crucial to invest when the startup has exited the infamous “valley of death” and is starting to see success with its ventures, but before the company becomes large enough to devalue future funding, as mentioned above. Many new mental health startups

founded around the start of the pandemic have reached the pristine stage for VC investment. Now may be the best time to invest.

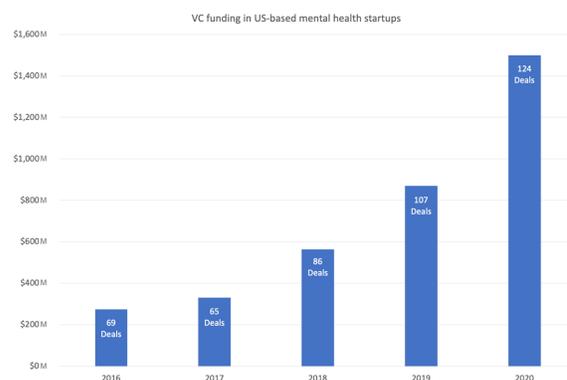


Figure 2. VC deals in mental health startups from 2016 to 2020 (Source: Forbes)⁹

Case study: Kaiser Permanente

On the other hand, companies like Kaiser Permanente have been less successful in the mental healthcare sector. Though a healthcare giant, Kaiser has been repeatedly accused in the past of denying mental health treatment to its clients, for which it was fined \$4 million in 2013. The COVID-19 pandemic has only worsened the issue. Kaiser’s flawed appointment system and the lack of funding and personnel devoted toward mental healthcare, problems which it has long failed to fix, coupled with the skyrocketing demand for care during the pandemic left them completely overwhelmed. Urgent appointments were delayed for months, leaving patients with utterly unsatisfactory care.¹⁰

Kaiser Permanente is a prime example of a company that has failed to innovate to adapt to the post-pandemic mode of mental healthcare service. The pandemic provided an invaluable opportunity by multiplying demand for the company’s mental health services, a situation Kaiser as a healthcare giant with ample capacity was perfectly poised to take advantage of. Success was knocking at the door; failure was

completely inexcusable. Instead of expanding and reforming its operations, Kaiser persisted in its old ways, causing the pandemic's benefit to become a detriment.

VC investment in such companies should be conducted with caution for 3 reasons. Firstly, poor performance and customer dissatisfaction indicates a lack of growth potential. Secondly, the large quantity of legal fines should be a red flag, as investment funds may be used to pay those fees instead of helping the company grow, reducing the future returns. Lastly, the fact that Kaiser failed to take advantage of and adapt to the pandemic is a sign that it will miss other profitable opportunities as well.

A Grain of Salt

As with most industries, mental healthcare VC investment comes with a risk. There are signs that the explosive growth in digital mental health is unsustainable – investment in the sector dropped considerably across all quarters of 2022 compared to 2021. Though not ideal, this phenomenon is not as foreboding as it may seem, because 2021 was anomalous in its high funding, and investments this year are still exceeding those in 2020.¹¹ Still, this raises questions as to whether the innovative solutions offered by startups are long-term and not just a sudden craze which would dissipate after the COVID-19 pandemic, and whether the upward trend in mental health can be maintained.

Conclusion

The state of VC investing in the post-pandemic mental healthcare sector is precarious but undoubtedly worthwhile. Mental health in large part consists of aspects outside of the control of individual investors, such as healthcare law, therapists and insurance. But

these risks are inevitable in investing, and can be mitigated by sufficient due diligence. Investing in mental healthcare is not only a good opportunity to earn money, but also to contribute to the wider society. It has been shown to boost innovation, enhance wellbeing, and improve productivity. Thus, when creating one's investment portfolio, it would be wise to consider mental health as a potential course for investing.

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