PUBLIC SECTOR INFLUENCE ON PRIVATE FUND BEHAVIOR: GERMANY’S VENTURE CAPITAL INDUSTRY (SUMMARY)

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SUMMARY

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Principal Topic

Nowadays most countries understand the importance of a well functioning venture capital (V/C) industry for employment creation, innovation and economic growth. Recently, Germany launched a variety of programs to channel financial resources, particularly at early stage, to technology ventures through private V/C funds.

Research has shown that when V/C institutions, investors (either governmental or private) and fund managers hold different interests, important consequences can (and do) result. Different incentive structures written into contracts between them affect managers’ investment behavior (Gilson, 2003). When government makes co-investments alongside private investors, political goals might clash with strategies of return maximization on investments. Governments, as a general rule, seek social return (Jääskeläinen, et al, 2004).

This research starts from the premise of a possible conflict of interests between private investors and government as an investor in V/C portfolios (Becker & Hellman, 2005; Zacharakis, 2004; Leleux & Surlemont, 2003). It tests the hypothesis: (1) public sector finance influences the generation of V/C funds and the fund’s venture investment and exit timing; (2) private V/C funds with public sector financing experience will launch additional privately-invested funds and (3) public sector financing for the V/C industry provokes a crowding-out effect on investments in private V/C funds.

Method

We examined the perceptions of key actors in the V/C industry. A structured questionnaire was answered by 17 private V/C firms and institutions, 6 corporate V/Cs, 17 private financial institutions, 6 public sector V/C programs (federal and state levels), 5 private savings and loans institutions (Sparkassen), 3 quasi-public SMEs financial institutions (Mittelständische Beteiligungsgesellschaften – MBGs) and 17 V/C industry experts.

Results and Implications

Our research results confirm that government influences the composition of private V/C funds. They rejected, however, that government influences exit timing, in partial contradiction with Tykvova (2004). Next, the research did not find evidence for private V/C funds with experience in public cooperation launching additional funds, differing from Scherer (2000). Finally, it did not confirm the crowding-out effect. Our research develops a composite empirical test, providing understanding of specificities of public sector influence on private fund investment and exit strategy and contributing to the public sector crowding-out effect debate.

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