INVESTMENT STRATEGIES IN TRANSITION ECONOMIES: AN EMPIRICAL STUDY OF U.S. VENTURE CAPITALISTS IN CHINA (SUMMARY)

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SUMMARY

INVESTMENT STRATEGIES IN TRANSITION ECONOMIES: AN EMPIRICAL STUDY OF U.S. VENTURE CAPITALISTS IN CHINA

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Principal Topic

China is a developing economy that is also in transition from state-owned enterprises to free-market capitalism. While such dramatic change on such a grand scale has given rise to many new opportunities, it also presents new challenges and risks, especially for outside investors. As a developing economy, China has underdeveloped institutions (Ahlstrom & Bruton, 2006; Scheela, 2006). As an economy in transition, China is experiencing the destruction and transformation of existing institutions with high uncertainty and instability.

Kambil, Long, & Kwan (2006) proposed seven disciplines critical to successful investment in China, such as knowledge of the legal structure and an ability to navigate complex regulatory environments. Institutional theorists add social and cultural elements by suggesting that networks and social capital (Guanxi) substitute for key formal institutions such as the rule of law (Ahlstrom & Bruton, 2006). Agency theory explanations of the role of venture capital seem to encounter some new twists in the emerging and transitioning institutional setting of China (Zeng, 2004). However, there are few empirical studies of venture capital in China based on these frameworks.

In this study we look at whether and how VC’s have modified their approach from the “Silicon Valley” model (Cannice & Daniels, 1999) in order to deal with the situation in China. In particular, we are interested in whether the VC strategies in China can be explained from an institutional or agency theory framework.

Method

A questionnaire was distributed to the 350 plus Chinese and foreign (U.S. and other) venture capital firms in that are members of the ZerotoIPO network. The questionnaire addresses a number of important questions: (1) How do U.S. venture capitalists perceive the institutional setting in China? (2) What kinds of ventures are they investing in (state-owned versus private, startup versus later stage)? (3) How do they conduct business differently at each stage?

Results and Implications

Preliminary results indicate that foreign VC’s find the environment more risky in China and that they have adopted a number of strategies to deal with the underdeveloped and transitioning institutions, including greater reliance on personal networks.

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