PROXIMITY IN INFORMAL VENTURE CAPITAL INVESTING – WHAT DOES IT MEAN? (SUMMARY)

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SUMMARY

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Principal Topic

Informal venture capital (IVC) market, which consists of private individuals investing equity capital in unquoted ventures to which they don’t have any family connections, has often been described as a local market. Individuals tend to invest in their geographical proximity for several reasons, including the local nature of information on potential deals, the need to monitor due to agency risk and informal investors’ tendency to engage in post-investment involvement. What has not been given much attention in the literature is why, given the importance of geographical proximity in IVC investing, a considerable portion of IVC investments nevertheless occur over distance? This paper sets out to explain the role of proximity in IVC investments, aiming to contribute to better understanding of spatial dynamics of IVC market.

The argument developed in this paper is that the need for geographical proximity is context-dependent and relies on the setting in which the investment is undertaken. I argue that geography is only one of the multiple dimensions of proximity and can be fully or partially substituted by non-spatial dimensions of proximity. Those are: social proximity (socially embedded relations between actors); cognitive proximity (shared knowledge, understandings and language); and institutional proximity (common habits, routines, established practices and rules of behaviour).

Method

The theoretical argument is tested on data from a large random sample of IVC investors, containing 278 informal investors and information about 422 of their investments, and in the second stage verified by in-depth qualitative interviews with theoretically sampled informal investors.

Results and Implications

The results show that social, institutional and cognitive proximities reduce the negative effect of geographical distance on the probability of informal investment. The relationship is, however, more complicated, as the perception of geographical proximity varies in different investment situations. IVC investments can be classified in three categories with respect to the role that geographical distance plays: locally situated, where the local nature of investment is one of the main rationales behind undertaking the investment; professional rationalistic, where the lack of geographical proximity can be compensated by higher returns as well as non-spatial proximities; and alternatively motivated, that is characterized by neutral relation to geographical distance.

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