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CARROT AND STICK: IMPACT OF EARLY-STAGE VENTURE CAPITALISTS ON THE PERFORMANCE OF VENTURES (SUMMARY)

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SUMMARY

CARROT AND STICK: IMPACT OF EARLY-STAGE VENTURE CAPITALISTS ON THE PERFORMANCE OF VENTURES

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Principal Topic

This research examines the manner in which venture capitalists affect ventures’ performance. In particular the underline question is to understand whether venture capitalists select or create winners. To start answering this question we examined how the early-stage syndication strategy and post-investment activities affected separately and simultaneously ventures’ performance.

We hypothesised that early-stage syndication shall diminish the adverse selection problem due to the information sharing between the investors (Bygrave, 1987; Lerner, 1994) and hence increase the chances that the chosen venture be successful. We argued that the CEO replacement, unlike what was predicted by the agency theorists (i.e. Jensen & Meckling, 1976) is a means for VCs to inject missing managerial competences into the venture (Bruton et al., 2000; Wasserman, 2003) and the later the replacement is done, the less is the loss of the information advantage (Bygrave, 1987) hold by the CEO-founder, the more positive will be the impact of the replacement. We also hypothesised that the resource provision functions (Pfeffer & Salancik, 1978) will increase the venture’s performance. Finally, we postulated that the early-stage syndication will positively moderate the effect of the VC’s involvement if the value-added argument prevails (Brander et al., 2002) and negatively, if the VC behaves as a free-rider (Dimov & De Clerq, 2006) or the coordination costs among co-investors are too high to take decisions efficiently.

Method

We drew our analysis on a unique hand-collected data set. We collected data by the means of questionnaires from early-stage VCs on each portfolio company they hold. An exceptionally high response rate of 72% provided us with complete data on 221 ventures.

Results and Implications

Regression analysis revealed that ventures that outperformed others were those that had been selected at the early-stage of development by at least two venture capitalists and then received advice and benefited from other resource provision related activities of the venture capitalists during the post-investment process. Our result showed that neither careful selection nor active post-investment involvement is self-sufficient to assure high ventures’ performance, providing support for the existence of resource-sharing among co-investors.

Our results provide an original reassessment of the agency and resource dependence perspectives in the context of venture-capital backed ventures and advance further the literature regarding the venture capitalists’ role and impact on the ventures’ performance. We believe that our finding also provides some useful insights for venture capitalists and entrepreneurs.

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