ENTREPRENEURIAL TEXT, PRIOR KNOWLEDGE, & INVESTOR INTEREST (INTERACTIVE PAPER)

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INTERACTIVE PAPER

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Principal Topic
When venture capitalists screen investment opportunities, they often select projects for further consideration based on cursory reviews of written business plans or executive summaries (Hall & Hofer, 1993; Hisrich & Jankowicz, 1990). Conventional wisdom instructs entrepreneurs to minimize uncertainty in their business plans by removing any “unaddressed cracks, flaws, or gaps,” yet there has been little systematic research on whether the nature of the text entrepreneurs present affects the investment screening decision. Our paper examines whether characteristics of entrepreneurial text affect investment screening decisions, depending on prior domain-specific knowledge of investors. We extend prior research on venture capital decision-making by focusing on more fine-grained elements of the screening process, linking the characteristics of the text describing the investment opportunity to the knowledge of the investor.

Research in cognitive psychology has established a relationship between readers’ prior knowledge, text coherence, and the level of active processing that occurs (McNamara & Kintsch, 1996). Greater background knowledge has been shown to increase readers’ interest in the material (Alexander, Kulikowich, & Schutze, 1994; Tobias, 1994). This research has found that low-coherence text causes high-knowledge readers to “fill in the gaps” with their own experiences, thereby engaging with the text at a deeper level.

We introduce the idea of conceptual coherence to describe the logical completeness of texts. We define conceptual coherence as the extent to which the underlying thinking in a text is articulated, with assumptions clearly laid out and detailed logic linking the assumptions with the conclusions. Specifically, we hypothesize a main effect that texts describing entrepreneurial opportunities will be more interesting for investors with domain-specific knowledge (that is, knowledge relevant to the industry or entrepreneurial idea described in the text) than for other investors.

Methods
To test our ideas, we conduct an experimental study involving 50 venture capitalists. The study uses a repeated measures design, where participants are presented with texts describing identical investment scenarios with varying degrees of conceptual cohesion.

Implications
In practical terms, our study suggests that early-stage entrepreneurs, whose ideas may be low in conceptual coherence, should target their pitches to well-matched venture capitalists and should do so in a way that engages the venture capitalists’ expertise without undue attention to conceptual coherence. As their ventures develop and their business plans become less ambiguous and more conceptually coherent, this match may be less important.

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