DRESSING UP FOR A BIG WEDDING: THE IMPORTANCE OF LEGITIMACY BUILDING WHEN REALIZING AN EXIT BY TRADE SALE (SUMMARY)

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SUMMARY

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THE IMPORTANCE OF LEGITIMACY BUILDING WHEN REALIZING AN EXIT BY
TRADE SALE

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Principal Topic

The venture capital literature suggests that the most likely exit for a VC investing in a young technology-based firm is a trade sale. In line with this empirical observation, an increasing number of scholars have investigated the determinants of a successful acquisition. However, most of the received literature analyses acquisitions from the perspective of the acquirer and focuses on managerial actions that are likely to increase the acquisition success for the acquirer. In this paper, we take the perspective of the young technology-based firm and analyze to what extent managerial actions undertaken by these firms have an impact on their likelihood of being acquired and their eventual acquisition price.

To analyze management’s strategic actions that optimize both the acquisition likelihood and the acquisition price, we build on legitimacy theory (Singh, Tucker & House, 1986; Suchman, 1995). Institutional theories have long recognized that institutional norms can be subject to purposive manipulation by organizational agents (Aldrich & Fiol; 1994; Lounsbury & Glynn, 200; Zott & Huy, 2007). Young technology-based firms are expected to actively manipulate expectations to gain legitimacy. Gaining legitimacy is important for entrepreneurial ventures since the crucial motivator of external parties to provide the new venture with resources is the belief that the young technology-based firm is indeed legitimate (Zimmerman & Zeitz, 2002).

Method

To test our hypotheses, we constructed a unique sample of 296 young technology-based firms, located in the UK. All firms in the sample were founded between 1991 and 2004 and develop and commercialize new products or services based upon proprietary technology or skills. Based on secondary data sources, we collected information on financing history, past performance and legitimacy building actions (such as getting media coverage, engaging in partnerships etc) of these young technology-based firm.

Results and Implications

The results indicate that different forms of legitimacy play a role in the success of realizing a trade sale. Our analyses reveal that having a VC on board with experience in realizing trade sales, hiring experienced top managers and patenting positively affect the acquisition likelihood. The acquisition price on the other hand is positively affected by these legitimacy building actions: having numerous partnerships and gaining media coverage.

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