FAILING TO LEARN OR LEARNING TO FAIL: CONSEQUENCES OF FAILED INVESTMENTS FOR VC SYNDICATION STRATEGIES AND PERFORMANCE (SUMMARY)

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SUMMARY

FAILING TO LEARN OR LEARNING TO FAIL: CONSEQUENCES OF FAILED INVESTMENTS FOR VC SYNDICATION STRATEGIES AND PERFORMANCE

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Principal Topic

Failure is an important component of entrepreneurial endeavors which has been given disproportionately little attention in the entrepreneurship literature, and especially in the venture capital context. This is unfortunate, because experiencing failure can open possibilities for significant learning, which can improve likelihood of future success.

In this paper, we study failure in the context of VC syndication and argue that the investment process preceding a failure offers not only valuable lessons about improving the VC’s future operations, but also an intimate understanding of syndicate partners’ behavior under conditions of adversity. Pre-failure cooperation offers unique opportunities for building relationship-specific assets among partners in the syndicate because firms ordinarily do not subject their norms of operation and coordination to the same scrutiny when succeeding as when things start deviating from the expected. Accordingly, in this study we rely on literature on learning from failure to develop a theoretical model with hypotheses specifying the conditions that make the renewal of a relationship between syndicate partners following a failure more likely, and how such renewed syndicates affect the post-failure investment performance.

Method

This research draws on the VentureXpert database. We consider all venture-related syndicated first-round investments in U.S. companies made by U.S. VC firms during 1980-2008 and distinguish between failed and successful investments.

Results and Implications

The results of this research are in preliminary stages, yet already offer unexpected insights into the consequences of failure for syndication renewal and subsequent performance of renewed syndicates’ investments. In acknowledging that not all failures are equal, we expected to find that the duration of investing period prior to failure would have an inverted U-shaped relationship with the likelihood of syndicate renewal. Instead, we find the hypothesized effect for the syndicate duration, yet no support for the distinction between failed or successful investments. In addition, we expected that renewing partnerships with a history of failed relationships would have positive effects for subsequent performance, yet preliminary findings show no effects for the prior syndicates’ outcomes, be they successes or failures. However, the results support prior research on relational capital in finding a strong positive effect of collaborative history in a partnership for subsequent performance. While necessarily speculative, the non-significance of expected relationships leads us to offer a series of recommendations in pursuing future research on failure in the context of VC syndicates. More refined analyses of our theoretical model are underway.

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