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NON-FINANCIAL WARNING SIGNS OF PENDING FAILURE: MEDIA ATTENTION (SUMMARY)

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≈ SUMMARY ≈

NON-FINANCIAL WARNING SIGNS OF PENDING FAILURE: MEDIA ATTENTION

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Principal Topic

Much research has been done on the signs of new venture failure. However, most studies are focused either on inherent or pre-determined factors of a startup (such as the qualifications and/or experience of the management team) or hindsight factors assessed in a startup's post-mortem. The research that addresses current signs of failure—while a startup is operating—is mostly financial in nature, focusing on monitoring a company's revenue-to-cash conversion, indebtedness, etc. This paper focuses on evaluating the effectiveness of a nonfinancial warning sign of pending new venture failure—the level of media attention received.

Method

Twenty startup companies were selected from the portfolio of a well-known Boston-based venture capital firm – 10 failures and 10 successes – that the firm invested in over the past 10 years. Successes were defined as companies that were exited by the VC firm through an IPO or a sale that returned more than two times the cumulative investment. Failures were defined as companies that were either exited at a return multiple of less than two or have generated no liquidity event after an excess of six years. The number of media mentions, as present in Factiva's database, as well as the timing and sources of those mentions were recorded for each company between the period of investment and exit or December 31, 2010, whichever came first.

Results and Implications

There is a statistically significant difference in the patterns of media attention between failed companies and successful ones. Successful companies have on average 250% more articles in which they are mentioned—across all time spans: weekly, monthly and annually—than their failed counterparts. For example, failed companies showed an average of 0.8 mentions per week, as compared to successful companies, which showed 2.8 per week. Even more striking are the differentials in growth rates. The average annual growth rate of media mentions for failed companies was 32%, while the average rate for successful ones was 209% — a 551% difference.

The implication of this paper is the presentation and assessment of a potential signal of failure that has previously not been widely focused on. The correlations between content frequencies, sources, and patterns of media mentions will hopefully provide a contemporary framework of leading indicators on measuring nascent venture success or failure. Simultaneously, this framework provides entrepreneurs and investors a way to evaluate the status of their companies and make appropriate decisions in a timely manner.

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