HOW TO CONCENTRATE LESS: FOREIGN AND CORPORATE VENTURE CAPITAL INVOLVEMENT IN SYNDICATES (SUMMARY)

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SUMMARY

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Principal Topic

Corporate VC (CVC) and Foreign VC (FVC) exhibit different risk exposure and risk mitigating approaches, one of which is syndication. The participation of corporate VCs (CVCs) or foreign VCs (FVCs) in financing rounds may impact investor concentration by affecting how other investors evaluate their investment risks. CVCs strategic investing in sectors with greater technological opportunities and weaker IP regimes (Dushnitsky and Lenox, 2005), reduces their investment risk through low resource commitment. Such investments facilitate established firms’ innovation efforts by exposing new technologies, risking expropriation of new ventures’ intellectual property (IP) that CVCs may exploit for their corporate gain. Other syndicate investors may thus limit investments due to similar concerns about CVCs’ expropriation of IP, creating more uncertainty and investment risk, and leading syndicate partners to eschew round dominance, thereby lowering investment concentration. As domestic markets become saturated with investors, VCs seek investment opportunities abroad, increasing cross-border investment contrasting with VCs home bias (Cumming and Dai, 2010). To mitigate foreign investment risks, FVCs usually participate in syndicates, but are less effective and less stringent than domestic VCs in selecting investments, leading to lower exit success. FVC participation may increase uncertainty in terms of venture quality for other syndicate investors. We thus test whether syndicates that include CVC or FVC investors have lower investor concentration in the round than syndicates without either.

Methods

Our sample consists of 1137 investing rounds for 354 companies founded from 1997-2003. Investor concentration is the Herfindahl index of individual round investors, and CVC Participation and FVC Participation are dummy variables indicating whether the round includes such investment. Controlling for venture, round, investor, and industry effects, we analyze the relationship between CVC or FVC participation and Investor concentration using a panel generalized least square regression analysis with random-effects.

Results and Implications

Investors are less concentrated in investment rounds when FVCs or CVCs participate, demonstrating that relational uncertainty resides both at the VC-venture dyad level and among the syndicate’s VCs. We demonstrate the consequences of CVC or FVC affiliation for new ventures and enrich our understanding of the investments provided by different types of VCs and their impact on syndicate partners.

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