THE IMPACT OF VENTURE CAPITAL AND ANGEL INVESTORS ON THE RELATIONSHIP BETWEEN FINANCIAL SLACK AND PERFORMANCE (SUMMARY)

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SUMMARY

THE IMPACT OF VENTURE CAPITAL AND ANGEL INVESTORS ON THE RELATIONSHIP BETWEEN FINANCIAL SLACK AND PERFORMANCE

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Principal Topic

The relationship between resource slack and performance is heavily debated and multiple theoretical frameworks and empirical studies provide contradictory insights (George, 2005). Prior studies on the relationship between slack and performance in entrepreneurial ventures have generally assumed that these ventures have similar shareholder structures or that different shareholders have similar preferences with regard to slack allocation, both of which are unlikely. Distinguishing between different types of shareholders is critical to enhance our understanding of the relationship between slack and performance (Kim et al., 2008). In this study we will focus on two important shareholders in entrepreneurial ventures, namely venture capitalists and angel investors. Through monitoring and active involvement in strategic decision making (Sapienza, 1992; Sapienza et al., 1996) these investors are likely to minimize some of the negative effects (including organizational complacency, over-optimism, and dampening incentives for experimentation) of holding too much slack as advocated by agency and resource constraints theories. We specifically focus on the following research question: How does the presence of venture capitalists (VCs) and angel investors (BAs) influence the relationship between slack and performance?

Method

In order to address abovementioned research question, we will use a unique longitudinal database containing detailed yearly financial accounts of 1,215 Belgian entrepreneurial ventures. We identified 120 VC-backed companies and 90 BA-backed ventures that received initial financing between 1994 and 2004. For each VC and BA-backed company we selected up to five comparable companies matched on company age, industry sector, and firm size.

Results and Implications

This study contributes to our understanding of the complex links between the presence or absence of resources and performance in entrepreneurial companies with high potential. We show that curvilinear relationships exist, not only between financial slack and performance, but also between human resource slack and performance. Both too much and too little slack in financial and human resources inhibit performance. More significantly, this study shows that the presence of venture capital and angel investors positively moderates the slack-performance relationship. This implies that private equity investors, as expert monitors, reduce the negative consequences of holding too much slack in entrepreneurial ventures.

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