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INTERACTIVE PAPER

THE STRINGS ATTACHED TO OTHER PEOPLE’S MONEY: OPPORTUNITY TYPES AND NEW VENTURE FINANCING

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Principal Topic

Opportunity research has been described as the distinct domain of entrepreneurship (Shane and Venkataraman, 2000). More recently, two types of opportunities have been described: discovery and creation (Alvarez and Barney, 2007). While these types of opportunities have been described theoretically, there has yet to be an empirical test of these opportunity types. This paper offers a first empirical test of these opportunity types by focusing on their implications for financing.

Method

Discovery opportunities are able to obtain formal financing from banks, angel investor groups and venture capital (VC) (Alvarez and Barney, 2007). This formal financing enables firm growth (Bradley, Wiklund and Shepherd, 2010). Creation opportunities, on the other hand, are limited to informal financing such as the proverbial friends, family and fools. This type of financing enables flexibility in these opportunities that allows for evolution (Bhide, 1994).

Distinguishing between opportunity types offers challenges to measurement as opportunities are unobservable (Godfrey and Hill, 1995). To overcome this obstacle, this paper creates a factor to measure the “degree of discovery” in an opportunity. The observable characteristics are based on the underlying assumptions of discovery and creation opportunities. Once opportunities have been distinguished, this paper measures the effect of formal financing, specifically VC financing, on firm performance.

Typically, most creation opportunities would not be able to obtain VC financing. Thus, to generate sufficient sample of creation opportunities with VC funding, the paper uses the time period of the dot com boom as a natural experiment. In this time period, VC firms invested in a much broader spectrum of opportunities – many of which would not have typically received VC funding.

Results and Implications

The results broadly suggest that a mismatch between opportunity type and exploitation strategy is correlated with decreased firm performance. Specifically, the implications for firm financing suggest that creation opportunities would be well served to avoid formal financing as the strings attached to those funds can lead to decreased firm performance. Finally, the study outlines boundary conditions between discovery and creation opportunities providing a first empirical test of the opportunities simultaneously.

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