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DIFFERENT SOURCES OF VENTURE CAPITAL AND THEIR INVESTMENT MANAGEMENT PRACTICES

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Principal Topic

Venture capital (VC) provides financing for new ventures (NVs) primarily in high-technology industries. Venture capitalists (VCs) investment practices manage information asymmetry and agency risks associated with these industries (Gompers, 1995). Corporate VC (CVC) investments by established firms provide differential value associated with NV performance (Gompers & Lerner, 1998). VCs prefer domestic investment (Cumming & Dai, 2010), thus foreign VC (FVC) investors may utilize specific investment practices to mitigate foreign investment risk.

Hypotheses and Methods

Round size is instrumental in investment risk mitigation (Gompers 1995). CVCs provide access to distribution channels and manufacturing facilities, and develop networks that enhance NV legitimacy, reducing liabilities of newness, and increasing the likelihood of success. Investors perceive CVC receipt as a positive signal of the NV’s quality, increasing overall round size. VCs high selectivity when investing cross-border suggests that FVC syndicate participation indicates higher venture quality, reducing investors’ risk perceptions and increasing willingness to invest.

H1(H2): Syndicates including CVCs (FVCs) disburse more funding per round than those without CVCs (FVCs).

Established companies may enhance their innovation activities by NV investing (Dushnitsky & Lenox, 2006), prompting ventures’ fear of innovation expropriation, increasing investors’ information asymmetries, and raising the potential for entrepreneurs’ opportunistic behavior (Eisenhardt, 1989). Investors adjust their interaction frequency with entrepreneurs to address goal incongruence (Sapienza & Gupta, 1994), using rounds to obtain information on the NV’s performance. FVCs’ greater distance challenges monitoring, increases the potential for opportunistic behavior and heightened agency problems, and leads to more intensive monitoring.

H3(H4): The involvement of CVCs (FVCs) in a round is associated with shorter inter-round intervals.

Methods and Results

NV and VC data from VentureXpert/SDC Platinum and CorpTech comprises 962 investing rounds for 334 private, U.S.-based, VC-backed high-technology NVs founded from 1997-2003, tracked in a panel data methodology. We model Round size and Round interval with Syndicate Type (CVC or FVC participation) using a panel GLS with random-effects and panel Poisson regressions. Syndicates with CVCs (FVCs) provide 103% (112%) more round funding than syndicates without CVCs, supporting H1 and H2. Syndicates with CVCs (FVCs) monitor more frequently than syndicates without these investors, supporting H3 and H4.

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