THE EFFECTS OF INITIAL FIRM CONFIGURATION AND VC INVOLVEMENT ON FUTURE FIRM GROWTH: A CASE OF PICKING OR FORMING WINNERS? (SUMMARY)

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Principal Topic

This study focuses on the long-term performance of new venture capital financed firms. Despite numerous studies on the value adding activities of VCs, few have actually managed to empirically confirm if and how VCs involvement in new firms actually has a positive effect on business performances, and especially on long-term firm performance. One can wonder whether the performance of VC financed new firms is an effect of skilled selection (picking winners) or good post investment management by the VCs?

The basic premise of “picking” is that it is possible for VCs to recognize the “best” new firms by looking at the initial firm configuration, and by this, select the most promising ones. As such, we could expect that (H1) the firm configuration at the time of VC initial funding have a long-term effect on its performance. Rather than just picking winners, VCs can form winners by taking an active governance role in the invested firms through active participation on the board of directors, acting as a sounding board, and monitoring financial performance. As such, we could also expect that (H2) VC involvement in a new firm during the investment period has effects on the long-term performance of a new firm.

Method

A population of 282 portfolio firms was generated from the database of Förvärv & Fusioner AB, which is a well-respected agency conducting research on mergers and acquisitions in Sweden. We collected data about these venture capital backed young firms using different methods over a ten-year period. Our final sample consists of over 100 entrepreneurial firms over their full venture capital cycle, that is, from the very early first investment to the exit.

Results and Implications

Our preliminary analysis seems to indicate support only for the H2, but in non-expected fashion: the more VCs are involved, the lower is the long-term performance of the firm. Contrary to our original argument, it might be that VCs have the “fire-fighter” role: VCs allocate their scarce time to funded firms with problems. When things go well, VC do not have to get so much involved.

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