

≈ SUMMARY ≈

**DO TOO MANY COOKS SPOIL THE BROTH? THE EFFECT OF SYNDICATION ON THE PERFORMANCE OF VENTURE CAPITALISTS' PORTFOLIO FIRMS IN SWEDEN**

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**Principal Topic**

The literature surrounding venture capital firms' relations to their portfolio firms is vast, but tend to focus primarily on the relationship between venture capitalists and entrepreneurs from the venture capitalists' perspective. Many studies focus on how the venture capitalists need to control their investment. It is often implied that venture capitalists are beneficial to the firms in which they invest. In several studies it has been suggested that venture capitalist add value to their portfolio firms by providing capital as well as competence in form of advice and improved routines to the portfolio firm. Many researchers seem to assume that venture capital firms' advices to portfolio firms are always relevant and useful. Governments and government agencies also tend to unconditionally support the venture capital industry as being crucial providers of venture creation. As Sweden has targeted science-related ventures as being of prime importance to the growth of the Swedish economy, venture capital provision has been placed in the forefront of likely contributors to venture growth in that particular field. Not all entrepreneurs seem equally impressed by contributions made by venture capitalists. Case research provides evidence of venture capitalists having a short term focus, lack of patience with investments and above all, being unable to provide adequate support in terms of contributions aimed at enhancing ventures abilities to market their products. According to these studies there seems to be indications that venture capital may not be as beneficial to venture growth as has been previously reported.

**Methodology/Key Propositions**

We have drawn a random sample of 100 venture capital backed ventures in Sweden and compared them with a control group of 100 non venture capital backed ventures. The ventures were sampled from a Swedish database comprising of more than 1700 investments made venture capital firms. The investments that were subject to analysis were being made in the period 1998 – 2001 and we followed the investments for three years. The same procedure was applied to the control group.

From the database that me made the random sample we have excluded MBO/MBI investments since they are outside what Bygrave & Timmons (1992) labeled "classic venture capital". The value added by venture capitalists in these re-structuring investments are primarily of a financial character and hence not of interest when compared to early stage and expansion investments.

It can be argued that venture capitalists' portfolio firms ought to come out ahead in a comparison with ventures lacking support from venture capitalists due to (1) the fact that they are able to cherry-pick ventures out of the population of viable firms and (2) because of the contributions in finance and methods of enhancing growth of firms. On the other hand, venture capitalists tend to take higher risks than other financiers, and are therefore likely to also suffer more in the event of an economic downturn. We have therefore tried drawing our non-venture capital backed firms from a sample that in terms of industry, size, etcetera, closely matches the

sample of venture capital supported firms. We have also selected a timeframe over a cycle of both economic upturn and downturn.

### **Results and Implications**

The preliminary results from this study (more data will be available at the time of the full paper enclosure) indicate that venture capital firms to a slight degree are able to generate growth for the firm they finance, however this seems to be more tied to the fact that they provide capital than to their ability to actually contribute methodologically through added value. In general, support from venture capital does provide a boost for firms in which they invest, but also leads to far greater risks for the firm accepting external venture capital. Combined with the turmoil reported by entrepreneurs dealing with venture capitalists it may be argued that the growth generated may not be able to offset the negative effects of having to deal with intrinsically shortsighted and impatient investors. Based on this study it is doubtful if the venture capital industry as it has functioned during the last ten-year period has provided reasons for governmental support. The value of the venture capital industry may be in the overall emphasis on internal structuring of ventures, such as the need for professional boards and external advice. This is offset by the added turbulence in the industry as venture capitalists tends to add towards “hype” in upturn markets, the lack of stamina in following up investments in downturn markets and the disenchantment of many entrepreneurs in dealing with external capital. The main implication of the study is to theoretically provide a gap in the lack of studies actually measuring venture capital performance, and doing this not entirely from an investment perspective, but from a perspective where the needs of entrepreneurs are in focus. The governmental perspective primarily includes the ambition to achieve long-term economic growth in small and medium-sized businesses and is less well served by short-term investors striving to maximize short-term profits by buying and selling shares in ventures. Therefore it is imperative to view the venture capital industry based on its ability to support long-term growth in the economy. The huge upheavals in the venture capital industry are not necessarily in the interest of either entrepreneurs or governments.

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