International Journal of Commerce and Management Research
ISSN: 2455-1627, Impact Factor: RJIF 5.22
www.managejournal.com
Volume 2; Issue 7; July 2016; Page No. 77-81

International venture capital

Pallvi Rani

Assistant Professor, DAV College Hoshiarpur, Punjab, India

Abstract

Venture capital is an international phenomenon. Every country is adopting this concept in one or another sense. US and China are leading in using of venture capital. Other countries are also using but these countries still facing many problems like lack of knowledge, deal flow and proper support network for entrepreneurial activities. If the government of countries will take initiative in promotion of venture capital industry then it could give benefits to the entire world. This paper shows the trends of Venture capital in Asia and outside Asia. Reasons for less penetration of venture capital in most of the countries are also highlighted in this paper.

Keywords: Venture Capital, Venture Capital Funding, FIVCIE, VCMC

1. Introduction

Venture capital is a specialized form of financial intermediation that provides funding to innovative new ventures with high-growth prospects (Da Rin, Hellmann and Puri, 2013). Therefore, VC firms largely invest funds provided by other institutions or by wealthy individuals. Institutional investors (banks, insurance companies, sovereign wealth funds, family offices, etc.) invest in VC as part of their allocation to 'alternative assets.' This is very important, because intermediation creates constraints and incentives that are quite different from those that one would observe for investors that contribute their own money.

2. Approach of Venture Capital in Various Countries

2.1 India

Like other countries, the concept of venture capital is defined in a broad manner in India under the SEBI Regulations: ' Venture capital fund' means a fund established in the form of a trust or a company including a body corporate and registered under these regulations which-

i. has a dedicated pool of capital,
ii. raised in a manner specified in the regulations, and
iii. invests in venture capital undertaking in accordance with the regulations.

'Venture capital undertaking' means a domestic company –

i. whose shares are not listed on a recognised stock exchange in India; and
ii. which is engaged in the business of providing services, production or manufacture of article or things, or does not include such activities or sectors which are specified in the negative list by the Board with the approval of the Central Government by notification in the Official Gazette in this behalf.

2.2 China

"Foreign-invested venture capital investment enterprise" (FIVCIE) as used in these Rules means a foreign-invested enterprise established within the territory of China by foreign investors, or by foreign investors together with companies, enterprises or other economic organizations registered and established under Chinese law (the Chinese Investors), in accordance with the Rules to be engaged in venture capital investment business. "Venture capital investment" as used in the Rules means a type of investment activity pursuant to which equity investments are injected mainly into high and new-tech enterprises that have not been publicly listed (the Investee Enterprises) and venture capital management services are provided in order to obtain capital appreciation benefits.

2.3 Malaysia

"Venture Capital Company (VCC)" and "Venture Capital Management Company (VCMC)" means a corporation that deals or manages investments in securities of venture companies, and is registered as a VCC or VCMC, as the case may be, under the Guidelines. "Venture company" means a company which utilises seed-capital, start-up or early-stage financing and –

i. in relation to VCC, is not listed on the stock market of any stock exchange; and
ii. In relation to VCMC, is not listed on the stock market of any stock exchange at the point of first investment by such VCMC.

2.4 Taiwan

The term "venture capital investment enterprise" as used in the Regulations refers to a company limited by shares, which conforms to the following conditions:

i. engages in venture capital investment business under the approval of Ministry of Finance;
ii. Specialises in making investments either in foreign or domestic technological enterprises or in other foreign or domestic venture capital investment enterprises; and
iii. Not only makes a direct investment in the invested enterprises but also assists in the management or supervision of such enterprises.

2.5 United Kingdom

In UK, the definition of venture capital is very broad and includes the business of carrying on any of the following:

i. investing in, advising on investments which are, managing investments which are, arranging (bringing about) transactions in, or making arrangements with a view to transactions in, venture capital investments;

ii. advising on investments or managing investments in relation to portfolios, or establishing, operating or winding up collective investment schemes, where the portfolios or collective investment schemes (apart from funds awaiting investment) invest only in venture capital investments;

iii. any custody activities provided in connection with the activities in (i) and (ii);

iv. any related ancillary activities.

Further, venture capital investment is defined as a designated investment which, at the time the investment is made, is:

i. in a new or developing company or venture; or

ii. in a management buy-out or buy-in; or

iii. made as a means of financing the investee company or venture and accompanied by a right of consultation, or rights to information, or board representation, or management rights; or

iv. acquired with a view to, or in order to, facilitate a transaction falling within (i) to (iii) above.

3. Literature Review

Venture capital firms raise money from individuals and institutions to invest in businesses that have a potential for yielding high returns on high risk investments (Shalman, 1990) [11]. Venture capital funds usually have limited lifetimes that are determined when the fund is formed (typically ten years, which can be shortened or lengthened by one year increments for up to three years) (Shalman; Gompers and Lerner, 1999) [6]. Venture capitalists or fund managers are usually general partners who control day to day operations while investors are limited partners, who only monitor fund activities periodically, and do not participate in the fund's day to day activities (Shalman; Gompers and Lerner, 1999) [6]. Investors can include private and public pension funds, endowment funds, foundations, corporations, wealthy individuals, foreign investors, and venture capital firm managers. Professionally managed venture capital firms usually are private partnerships or closely-held corporations (Shalman; Gompers and Lerner, 1999) [6].

Venture capital investments are not secured with collateral; rather, venture capitalists take an ownership stake (equity investment) in the privately held businesses in which they invest (Shalman). Traditional and still currently, the lion's share of investments by venture capital firms have been in companies touting early stage (new) technology-based products. Such businesses have the potential for a high failure rate but also for yielding dramatically large profits. Venture capitalists reduce risk by carefully evaluating the technical and business merits of proposed business plans. Ultimately, they only invest in a small number of the businesses which are candidates for investments. Risk is also reduced by holding a portfolio of young companies in a single fund, by partnering with other venture capital funds when investing in a business, and often by simultaneously managing multiple funds (National Venture Capital Association, 1999).

The ownership stake that venture capital firms generally take in their portfolio companies typically run in the 30-40% range. In return for their investment, venture capital firms have some type of "say in" or influence over business management decisions. Typically, venture firms have a seat on the board of directors for the portfolio company and are intimately involved with the company in which they invest.

In this regard, they provide company management with contacts and help in formulating strategies. Close relationships are maintained by visiting and talking to company management. According to Shalman, venture capitalists visit each of their portfolio company on average 19 times per year resulting in a 100 hours of direct (phone and in person) contact. The degree of control or influence over portfolio companies is perhaps the most controversial aspect of venture capital investing. Many entrepreneurs either do not seek or decline venture capital funding because of a fear of losing control of their business or new product ideas. This fear underlies the use of the term "vulture capital" by some with venture capital firms rumored to require up to80% ownership of the business in return for their investment capital. Venture capitalists reply by stating that they only require their fair share of company ownership (usually under 50%) and desire to influence rather than control firm decisions.

Venture capital firms ultimately receive some combination of profits and preferred shares or royalties in return for financing. Typically, venture capitalists and portfolio business management and other owners gain their returns when the business undergoes its initial public offering (IPO) or when it is sold to another firm. At that point the venture capital firm liquidates any interest that it holds in the portfolio company. Because of the risk that they face, venture capital firms expect a higher than average internal rate of return as compared to other types of investments. However, rates of returns are not only dependent on the success of the company in which they invest, but also on the performance of capital markets in general and the market for initial public offering of company stock in particular (National Venture Capital Association).

The venture capital industry as it is currently structured began its growth and development immediately after the end of World War II. Early industry leaders included the Rockefeller Family, George Doriot, who taught at the Harvard School of Business and is often called the father of venture capital, and Jock Whitney. Early products were often commercialized off shots of technologies developed during the war, such as Minute Maid orange juice concentrate and micro-electronic circuitry (India Infoline, 2001).

Venture capitalists typically have a common identity and share very similar interests, (Wade, 1995) [12], i.e., they constitute a "community of practice" (Brown and Duguid, 2000) [3] with commonly held norms and the sharing of information. This phenomenon helps explain the herd-like behavior of many venture capital firms, where investments by a leading firm in a new area is rapidly followed by invests made by others (Kenney, 2001).

Venture capitalists also belong to a broader business network of entrepreneurs, institutional investors, potential executives, law firms, and a variety of others who can provide access to services and information. A venture capitalist who lacks a well developed set of contacts is just another uninformed investor (Kenney, 2001). This network also extends to the organizational level, where venture capitalists can help build links between diverse organizations, such as universities, investment banks, and growth oriented companies (Florida and Kenney, 1988) [4]. This intricate network provides a flow of information for venture capitalists, thereby enhancing their information base and lowering the risk inherent in their investment strategies (Koh and Koh, 2002) [8].

4. Research Methodology

4.1 Objectives of the study

1. To explore the meaning of venture capital in different countries.
2. To compare the Venture capital Investment of Asia with world.
3. To find out the reasons for low penetration of venture capital investment in some countries.

4.2 Tools Used

It is an analytical study. Secondary data is used for attaining the objectives of the study. Various reports published by authenticated sources are studied for the analysis.

5. Reasons for low penetration of Venture Capital

5.1 Lack of knowledge

First, some economies usually lack the fast growing sectors that have received venture capital funding, such as computer software, telecommunications, medical devices and equipment, biotechnology, and networking and equipment (Pricewaterhouse Cooper, 2003, Florida and Kenney, 1988) [10, 5]. Rural and smaller metropolitan economies are much more concentrated in traditional economic sectors that generally provide lower rates of return on investment than found in newer economic sectors such as computer software development. Even when such opportunities do exist in more traditional, rural-based sectors (such as food processing), venture capital firms may lack the expertise to evaluate and advise businesses belonging to such sectors where they normally do not invest.

5.2 Lack of deal flow

Another barrier to the use of venture capital in rural areas is the lack of deal flow or the relatively few investment exchanges made between venture capitalists and portfolio firms (Barkley, 2003; Barkley and Markley, 2001) [1, 2]. Fewer and more geographically dispersed opportunities for investment mean higher costs per rupee of actual venture capital transaction. Good investment opportunities are more difficult to find, evaluate through due diligence, and to ultimately monitor after the deal is made.

5.3 Lack of a proper support network for entrepreneurial activities

Another barrier to the use of venture capital in rural areas is the lack of a proper support network for entrepreneurial activities in general in many rural areas (Barkley, 2003; Barkley and Markley, 2001) [1, 2]. Venture capitalists rely on well formed networks to facilitate venture capital deals, provide critical information flows to assess potential deals, and to support portfolio businesses. These networks both among businesses and between the business community and key organizations such as local universities are often lacking in rural areas. In particular, the ability of entrepreneurs to network with each other and provide advice and support is often limited in rural areas. Such networks facilitate the development of new ideas, and help fledging businesses get off the ground by obtaining needed support (Nolan, 2003) [9].

5.4 Lack of understanding

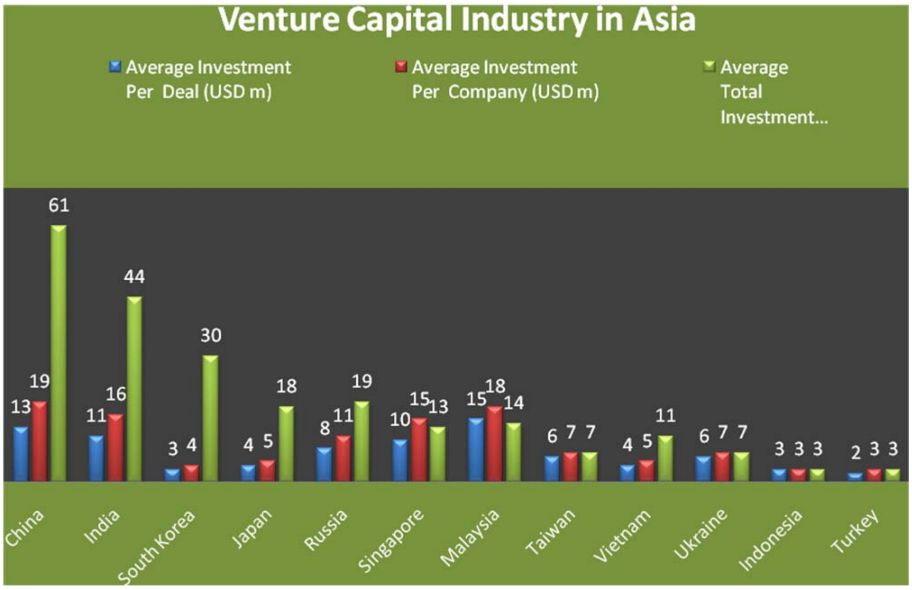
Another possible barrier not discussed in the literature but advanced by at least some managers of venture capital funds is a lack of understanding of the nature of venture capital held by many potential entrepreneurs in rural and small metropolitan areas. According to this viewpoint, such entrepreneurs have more access to venture capital than one might expect, but lack a clear understanding of its nature and requirements.

Several types of policies have been implemented in an attempt to circumvent the problem of lack of equity capital in rural areas. Markley (2001) [1] has termed these efforts as community development venture funds while Barkley uses the term nontraditional venture capital funds. In general, these attempts at providing venture capital to rural areas have met with, at best, mixed success.

6. Venture Capital Industry in Asia and Outside Asia

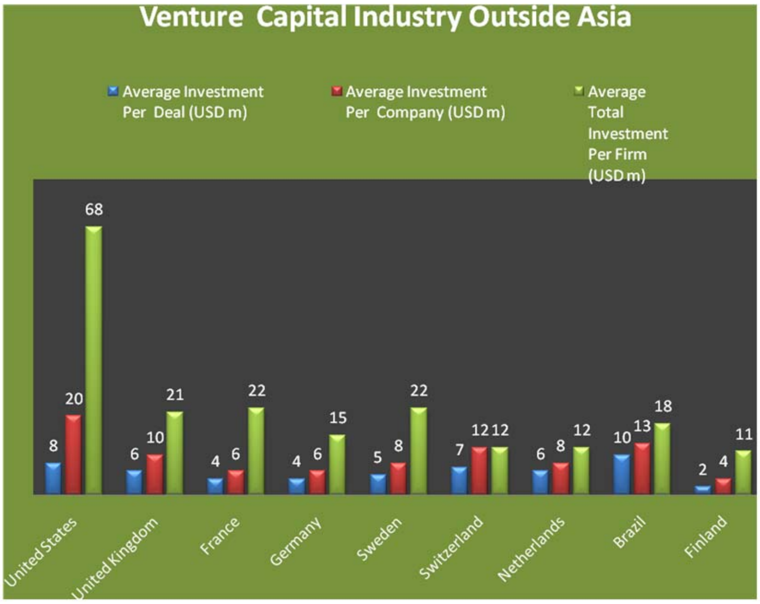
6.1 Venture Capital in Asia

Country Name	Deals (Total)	Companies (Total)	VC Firms (Total)	Average Investment Per Deal (USD m)	Average Investment Per Company (USD m)	Average Total Investment Per Firm (USD m)	Total Capital Invested (USD m)
China	6,284	4,467	1,350	13	19	61	82,721
India	2,169	1,407	522	11	16	44	23,103
South Korea	1,182	904	132	3	4	30	3,972
Japan	912	715	200	4	5	18	3,680
Russia	419	326	179	8	11	19	3,487
Singapore	286	199	231	10	15	13	2,973
Malaysia	47	40	49	15	18	14	701
Taiwan	109	88	95	6	7	7	644
Vietnam	69	59	28	4	5	11	299
Ukraine	32	29	28	6	7	7	198
Indonesia	52	43	50	3	3	3	134
Turkey	58	51	46	2	3	3	129



6.2 Venture Capital outside Asia

Country Name	Deals (Total)	Companies (Total)	VC Firms (Total)	Average Investment Per Deal (USD m)	Average Investment Per Company (USD m)	Average Total Investment Per Firm (USD m)	Total Capital Invested (USD m)
United States	41,018	16,807	5,017	8	20	68	338,940
United Kingdom	3,544	2,143	1,032	6	10	21	21,698
France	2,827	2,066	547	4	6	22	12,084
Germany	2,573	1,619	660	4	6	15	9,761
Sweden	1,158	753	286	5	8	22	6,198
Switzerland	453	263	261	7	12	12	3,165
Netherlands	521	364	256	6	8	12	3,024
Brazil	289	226	161	10	13	18	2,954
Finland	754	471	167	2	4	11	1,778



7. Conclusion

Venture capital is an international phenomenon. Every country is adopting this concept in one or another sense. US and China are leading in using of venture capital. Other countries are also using but these countries still facing many problems like lack of knowledge, deal flow and proper support network for entrepreneurial activities. If the government of countries will take initiative in promotion of venture capital industry then it could give benefits to the entire world.

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