

Quarterly Brief

Winter 2008/2009

In the Winter Quarterly Brief we present a comprehensive overview of the state of the economy and its impact on private equity. We review an interesting publication by Mike Wright and Riva Chopraa, which examines a number of papers looking at the performance of venture capital and helps dispel some of the myths around the industry. The Brief also provides an update of industry statistics, including fundraising and investment information. Finally, the latest activity within the BVCA Research Team is provided, including details of recent surveys on venture capital and mid-market debt.


The format of this bulletin is flexible, and we would welcome your comments and views to make it tailored to the needs of our members.



Roger Kelly
Chief Economist

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There is a need to remind the public of the benefits of the private equity model, and demonstrate that these benefits are generated without giving rise to systemic risk.

The Current Economic Environment

Economic conditions seem to be deteriorating on a daily basis, despite the best efforts of the authorities. The main drivers behind the current situation are the shutting down of the shadow banking system, resulting in a severe cutback in overall bank lending; the huge fall in demand as households and firms retrench; and the dramatic reduction in world trade.

The gravity of the current situation is exacerbated because of its synchronicity - it has affected all countries around the world, and led the IMF to recently describe the situation as the worst globally since 1945. They forecast that the world economy will suffer its worst performance for more than 60 years this year, with global output falling for the first time since WW2, in spite of inclusion of fiscal stimulus packages. Britain is facing the deepest recession of any big industrialised economy, according to the IMF report, which forecasts that the UK economy would shrink 2.8 per cent this year. This gloomy perspective is in line with the forecasts of the CBI and the Bank of England, although on a more positive note, the latter's central forecast, as published in the latest Inflation Report, suggests that we are already half way through the recession.

Although all major economies are negatively affected, they are not all affected in the same way. Countries can be divided into two broad categories. The deficit countries, characterised by large consumption-driven current account deficits, most significantly the US and the UK, are struggling in the face of falling domestic demand and rising unemployment. The woes of the surplus countries, such as Germany and Japan (and of course China), stem more from external factors, mainly plummeting exports due to decreasing world trade. Matters are made worse in Japan thanks to the huge rise in the value of the Yen on account of the unwinding of the carry trade, and weak domestic demand, which has never really recovered from the 1990s.

In order to address the crisis, governments have learned from the lessons of Japan in its 'lost decade' of the 1990s and acted quickly and decisively. Wide-ranging fiscal stimulus programs are being implemented in an attempt to replace falling private demand with public demand; programs are being introduced to clean up and recapitalise banks, and efforts are being made to restore trust in the system, and improve transparency. The size of the global response is on an unprecedented scale: weighted by their economies' size, the plans of 11 big advanced and emerging economies are worth an average of 3.6% of GDP, albeit spread over several years. And this does not include the upfront costs of financial rescues, including bank recapitalisations and guarantees of troubled assets. Including lost tax revenues and increased welfare costs, the IMF expects rich countries' combined fiscal deficit to rise to 7% GDP in 2009, from less than 2% in 2007.

But policymakers face something of a dilemma; the measures undertaken conflict with the medium term need to rebalance the global economy, with increased domestic saving rates in deficit countries and a shift towards more demand coming from overseas trade and less from domestic consumption. However, it is clear that the immediate priority is to prevent meltdown by addressing the crisis of confidence that is causing falls in spending and production. In the short term measures to boost saving and curb excessive consumption would be destructive. A co-ordinated global response would be far more effective than unilateral action; at present, some countries are doing much more than others. The commitment made by G7 finance ministers and Central Bankers in February to work together using a full range of policy tools is an encouraging step.

A big risk at the present time is protectionism. While the lessons of the 1930s are unlikely to be forgotten, and the existence of the WTO makes it difficult for wideranging protectionism to take place, some discontent has been sounded over measures that have been proposed, such as the car industry rescue package in France, and the Buy American provisions. And exchange rate movements could also result in counterproductive protectionist responses. Macroeconomic stimulus offers the best insurance against protectionism, as was recognised by policymakers at the G7 meeting. Boosting demand at home will reduce the temptation to divert it from abroad; this is an easier policy for surplus countries to implement than deficit countries.

In the medium term, recovery depends on confidence in the solvency of the government, the solidity of the currency and the soundness of the economy. The fiscal packages represent a gamble - albeit an unavoidable one - by governments on their credibility; the rising cost of insuring sovereign debt suggests that investors are seeing a growing risk of default in certain countries.

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What does this mean for the private equity industry?

Activity has fallen dramatically. According to CMBOR, the UK PE market dropped to its lowest level for over 13 years in the fourth quarter of 2008. The value of buyouts reached just £994m in Q4 compared to £5.6bn in Q3 and £5.7bn in Q4 2007. Overall, 2008 saw £19.1bn from 549 deals, a fall of over 58% on 2007's record figure of £45.9bn from 671 deals. This downturn in activity, coupled with widespread concern among investors about year-end valuations, is reflected in the price of listed PE shares, which are currently at large discounts to reported values of assets owned by funds.

A report by Boston Consulting Group (BCG) foresees that 40% of PE firms will collapse in the next few years, with portfolio businesses sold off and teams dissolved. We're starting to see some signs of retrenchment by PE houses; Candover recently announced that it would shrink a fund raised last year, and some large buyout houses including Candover, Permira and TPG have recently decided to return uncalled capital to investors. A number of PE firms are cutting their staff, particularly in more troubled areas such as retail.

Not all the news is negative, and not all current activity is reactive; some PE houses have been actively and successfully fundraising, and deals have been getting done. The difficult times in the primary buyout market has resulted in a number of trends, as PE houses continue to reinvent themselves.

First, there has been a noticeable change in the capital structure of the deals that are occurring. Equity-only deals are becoming more common; according to Unquote, around 40% of the buyouts taking place in the UK in the third quarter of 2008 involved no acquisition leverage. And mezzanine finance is playing an increasingly important role now that debt markets have closed up. Previously, when capital was plentiful and cheap, mezzanine couldn't compete.

Second, there has been a large increase in secondary market activity, and an associated rise in fundraising by secondary market investors. The downturn has given rise to an excess supply of investment opportunities, as investors seek to shrink their balance sheets. This is driving down market valuations - private equity sellers have in recent months reportedly been getting only about 50 cents in the dollar, and in some cases much lower, of the face value of their investments, compared with more than \$1 in 2007 and 80 cents in the first half of 2008 (see recent BVCA Research Note <http://www.bvca.co.uk/Research/Research-Notes>). Sales have been driven by the denominator effect, increased risk aversion in the face of valuation volatilities, balance sheet distress, and in some cases because of overcommitment to funds.

Third, as part of the continuing evolution of the industry, PE houses have increasingly moved into distressed debt investing, in order to generate equity-style returns, and also as an alternative route into acquiring a business. Secondary market debt is no longer perceived as overpriced, as had been the case until recently. A number of PE firms have raised distressed debt funds, including Alchemy, who reportedly think that 50-75% of all outstanding leveraged capital will default over the next four to five years.

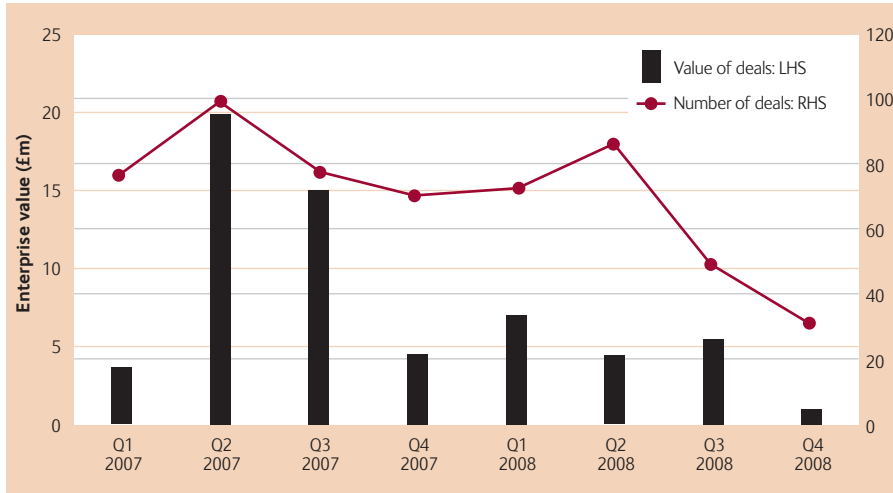
The fact that we are facing not just a financial crisis, but a crisis of confidence means that the private equity industry's response is critical. There are a number of questions that need to be considered, not least whether the business model still applies, but also how to create value in the current time and the new era, as it is likely that the economic environment post-crisis will be significantly different to that of the past few years. At the moment, private equity houses are focusing on what they can control: portfolio management seems to be the priority, and driving through operational improvements by working closely with management teams. There has also been a degree of crisis management, with PE houses focusing on managing cash and liquidity; making sure covenants are not breached, and attempting to reduce leverage in portfolio companies by buying back debt.

Further considerations include how to raise capital and deploy it effectively; and how to earn the public support of shareholders and governments. Private equity isn't really private any more, and there needs to be focus on stakeholders as well as returns. In this context, there is a need to remind the public of the benefits of the model, and furthermore to demonstrate that these benefits are generated without giving rise to systemic risk. Realistically, the PE industry is creative, and is constantly reinventing itself. Shakeouts occur in good times as well as bad. The current economic situation could benefit the industry, as private equity shows itself to be part of the solution, by providing much needed capital and expertise. ■

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Industry Statistics

The overall picture of the UK PE Buy-out market



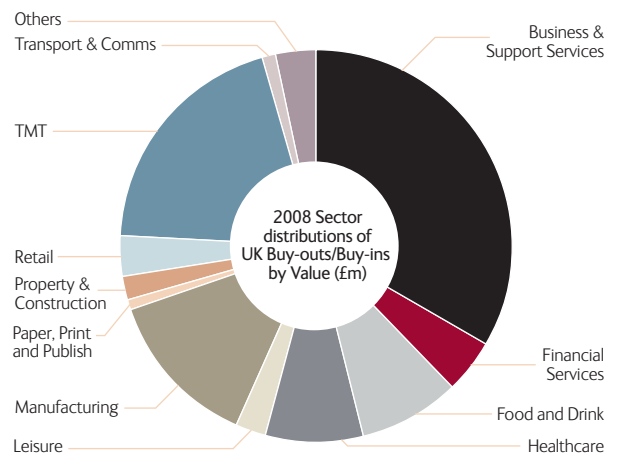
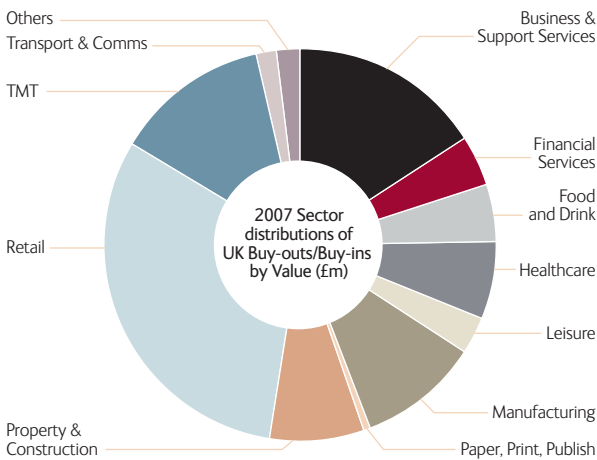
Investments

The last quarter of 2008 saw a massive drop in deal value, to the lowest level for over thirteen years, representing less than one-fifth of the deal value from Q3 2008 in the UK. The number of deals only fell by 37%, compared to the huge 82% drop in value, suggesting smaller deals are now of the essence as PE firms consolidate and focus on managing operational effectiveness to deliver returns.

Sector distributions of UK Buy-outs/Buy-ins by Value (£m)

| Sector Group | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 |
|-------------------------|------|------|------|------|------|------|------|------|-------|------|
| Bus & Support Services | 2261 | 1014 | 3568 | 1574 | 1393 | 4436 | 3486 | 2500 | 7326 | 6452 |
| Financial Services | 1354 | 519 | 528 | 772 | 582 | 889 | 2044 | 1541 | 1937 | 859 |
| Food and Drink | 1289 | 3743 | 668 | 906 | 492 | 769 | 205 | 3309 | 2131 | 1590 |
| Healthcare | 347 | 1504 | 552 | 1032 | 620 | 1481 | 4596 | 1145 | 2944 | 1560 |
| Leisure | 2120 | 3488 | 5631 | 4683 | 6162 | 3582 | 5178 | 5749 | 1433 | 477 |
| Manufacturing | 3770 | 4387 | 3446 | 1431 | 1284 | 2923 | 2962 | 2751 | 4518 | 2509 |
| Paper, Print, Publish | 297 | 609 | 149 | 70 | 911 | 158 | 200 | 145 | 317 | 164 |
| Property & Construction | 710 | 4283 | 2890 | 813 | 522 | 1366 | 470 | 2539 | 3542 | 358 |
| Retail | 1058 | 1456 | 638 | 2876 | 2352 | 2760 | 2629 | 3352 | 14343 | 619 |
| TMT | 1154 | 1151 | 590 | 482 | 1547 | 1182 | 1563 | 2236 | 5780 | 3776 |
| Transport & Comms | 226 | 843 | 212 | 237 | 450 | 450 | 229 | 1079 | 848 | 266 |
| Others | 2152 | 973 | 679 | 766 | 309 | 809 | 922 | 905 | 788 | 588 |

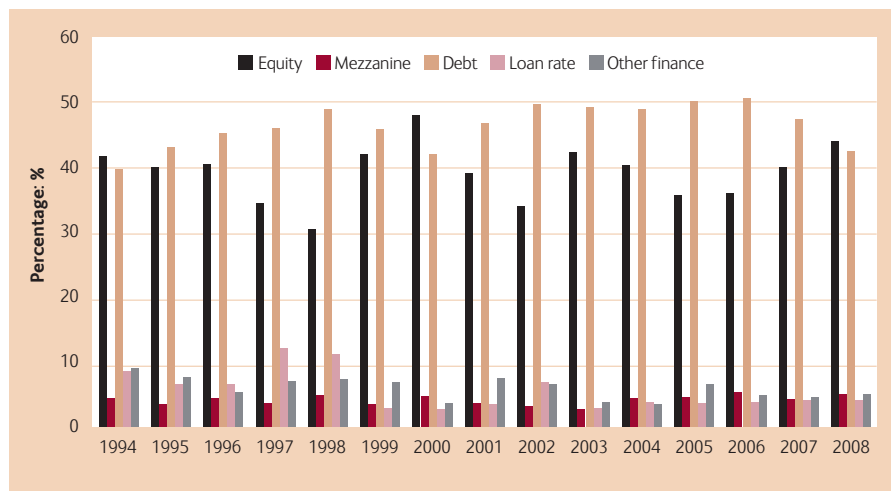
According to CMBOR, 2007 saw £45.9 billion invested from 671 deals, with 2008 figures falling to £19.1 billion from 549 deals. In a reversal of the recent trend, the business and support sector saw deals increase to 33.4% of total value, up from 16% in 2007 reflecting a similar absolute amount across the 2 year period. As would be expected, sectors with a greater susceptibility to market conditions saw a fall in activity, with the retail sector weighing in at only 3.2% of total value in '08, compared to 31.2% in '07, as highlighted in the two charts below.



Data provided by CMBOR.

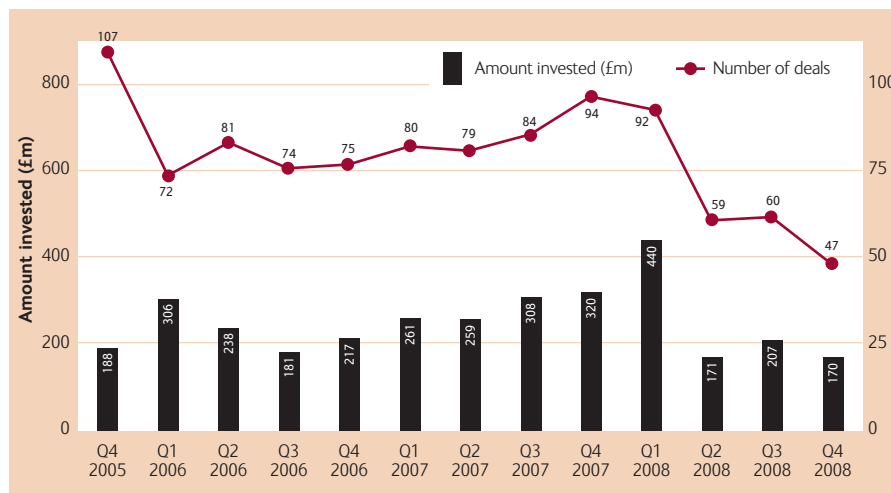
Debt levels of enterprise value fell fairly significantly from 47% in 2007 to 42% in 2008, decreasing to the lowest level since 1994 as depicted in the chart. Equity value increased to 44% in deals in 2008 from 40% in 2007, reflecting the problems in access to credit.

Deal Structure



2007 saw 337 VC deals in the UK worth in total £1.1bn, compared to 258 deals with a total value of £1.0bn in 2008. Q4 2008 saw 50% of the number of deals in the same period the previous year.

Trends in VC investment



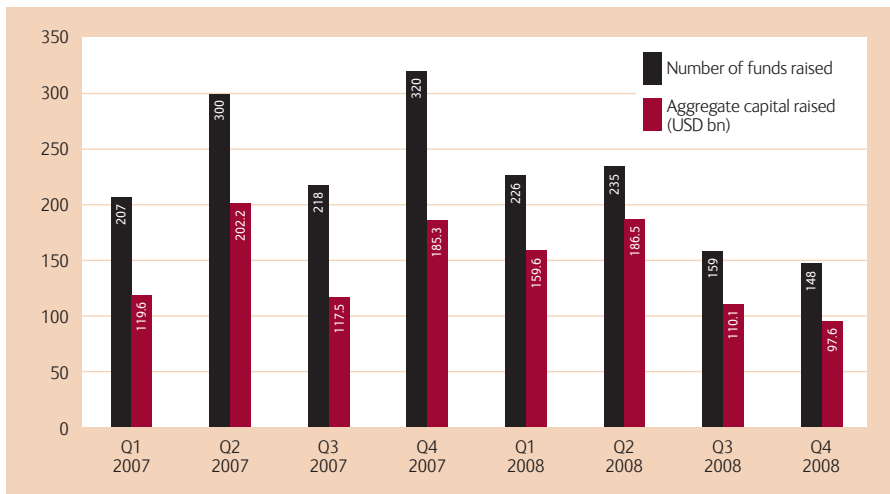
Source: Dow Jones VentureSource

Data provided by CMBOR.



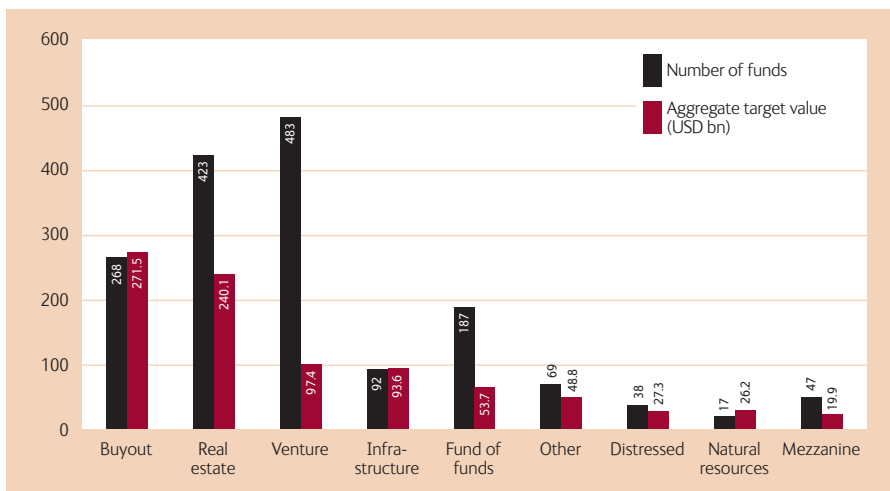
Fundraising

Quarterly Global Fundraising Q1 2007-Q4 2008



Fundraising activity has not suffered too adversely since the third quarter of 2008. With some LPs selling PE commitments, spectators may have thought that fundraising levels would be severely hit. But stronger performing primary GPs are still successfully raising funds and the strength of niche areas of PE, such as distressed and cleantech funds, demonstrates the adaptability of the industry.

Funds in Market by Fund Type



Buyouts continue to play an important role in the fundraising market. The increase in the number of funds of funds on the road could be attributed to the fact that LPs are looking to diversify their portfolio and see high returns potentially from these funds. Venture funds are the most active of funds currently raising, however this does not highlight how long these funds have been on the road. It is purported that committed versus uninvested capital in closed venture capital funds is at significantly low levels, as was discovered in a recent BVCA study, the preliminary findings of which are discussed on page 8. Indeed many of the VC firms surveyed believe the duration of fundraising activity will significantly increase due to difficulties in access to capital. **■**

Stronger performing primary GPs are still raising funds and the strength of niche areas of PE demonstrates the adaptability of the industry. **■**

Source: Preqin

BVCA Research Team Update

BVCA Annual Report on the performance of Portfolio Companies, 2008

Private Equity investment has brought a different ownership model and much higher levels of financial leverage to the portfolio companies in the sample. The findings of the research show that the effect of this on the performance of these businesses, from the date of acquisition to either exit or the latest annual accounts, has been:

- Organic growth in revenue and profits (EBITDA c7% p.a., revenue growth 3-4% p.a.)
- Organic growth in employment (3%)
- Investment in capital expenditure (less depreciation, 5% of fixed assets at date of acquisition)
- Investment in 'bolt-on' acquisitions (6% of fixed assets at date of acquisition)
- Limited disposals of assets (4% of the total at acquisition)
- On the investments that exited, strong investment performance was exhibited by strategic and operational improvements, over and above the benefits of additional financial leverage and market returns. (All 14 exits delivered positive Gross IRR to their investors and, overall, the aggregate investment return on the PE exits was 3.3 times, or 330%, of the return achieved by investors in the FTSE All Share in the same industry sectors and timeframes.) While about half of the return can be attributed to additional leverage, strategic and operational improvements under private equity ownership delivered an out performance of the 62%, over and above the FTSE All Share benchmark return at the same level of leverage.

As the research develops over time the data set will grow and the performance of Portfolio Companies over the broader economic cycle will be evidenced.

Venture Capital Survey, 2009

In a recent survey of BVCA Venture members with 80 respondents, 75% think that the number of investments and the amount invested will decrease significantly in 2009. For the 1,100 VC-backed companies in the UK, 84% of members had found it difficult in raising B and C rounds for these existing portfolio companies. When asked about the likelihood of achieving the next round financing for existing portfolio companies seeking capital, 74% thought it would be unlikely in 2009.

Given the concern for follow-on funding at existing portfolio companies, four-in-five (78%) members think they will have to write-off at least one company and one-in-three (36%) think they will have to write-off three or more companies in 2009 due to the lack of follow-on funding. The results are pretty similar when asked if they would have to write-off companies due to the worsening economic conditions as one-in-four (23%) will have to write-off 3 or more companies. Only 60% of members think they stand a chance for a successful exit for at least one company in 2009.

More than half of the respondents in the survey expect their average portfolio company in the product development stage to be able to survive 7-12 months on their current cash reserves if they cannot secure the next round of financing. Only 16% think they could last longer than 12 months and more than a quarter (28%) think they could not last longer than 6 months. Respondents are more optimistic about the time their average portfolio company that is already trading could last in the same situation, with one-in-three (36%) believing they will last longer than 12 months. However, almost half (45%) of members think they will last for 7-12 months, and one-fifth that they will last for less than 6 months.

When asked about a recovery in the IPO market, only 1% think it will recover in the next 6-12 months.

| | |
|---------------------|-----|
| Within 6 months | 0% |
| 6-12 months | 1% |
| 13-18 months | 40% |
| More than 18 months | 59% |

Three-fifths (59%) think that the recovery will take more than 18 months, while two-fifths (40%) think it will take 13-18 months.

Overall the aggregate investment return on the PE exits was 330% of the return achieved by investors in the FTSE All Share.

Four out of five (81%) members either found raising a fund more difficult or did not try to raise a fund because they knew it would be difficult over the last 12 months.

| | | |
|---|-----|---------------------|
| It is much easier to raise a fund | 0% | Easier: 0% |
| It is easier to raise a fund | 0% | |
| It is more difficult to raise a fund | 15% | More difficult: 67% |
| It is much more difficult to raise a fund | 51% | |
| We did not try to raise a fund as we know it is difficult | 14% | Did not try: 26% |
| We did not try to raise a fund for other reasons | 12% | |
| None of the above | 8% | |

Of these respondents, two-in-five (38%) have reduced the number of companies invested in as a result, while 17% have ceased new investments. One-quarter (24%) said it had not impacted on investments. BVCA members are almost unanimous in believing that the credit crisis will have an adverse impact on the ability of venture capital firms to raise additional funds from investors. 81% of members believe that the impact will be significantly adverse.

| | | |
|---------------------------------|-----|--------------|
| A significantly adverse impact | 81% | Adverse: 98% |
| A modestly adverse impact | 16% | |
| No impact | 0% | |
| A modestly positive impact | 3% | Positive: 3% |
| A significantly positive impact | 0% | |

For a full copy of the survey, please email research@bvca.co.uk with Venture Capital Survey in the Subject.

Mid-Market Debt Survey, 2009

Corporate banking relationships are likely to become increasingly strained over the coming months as the recession starts to bite and clearly many private equity portfolio businesses will be affected along with other public and private companies.

Many UK mid-market PE firms have already been involved in covenant reset and/or restructuring negotiations with the banks. Having spoken with a number of mid-market houses, it is clear that there is a growing concern about the banks' general attitude to such negotiations. It appears that in many instances the banks have been extremely hostile whilst in other cases the banks have been unable or unwilling to respond on a timely basis. It seems that some of the banks' workout teams are under great pressure due to a lack of resources (and this will only get worse as the number of under-performing companies increases). Also, the banks do not seem to have a coherent or consistent approach to restructuring/covenant-reset negotiations.

Clearly, if an investee company breaches its covenants then the banks are entitled to enforce their contractual rights as they see fit. However, the BVCA Mid-Market Committee believes the banks' current approach often actually leads to a worse outcome for themselves as well as adversely affecting other stakeholders such as employees or government creditors. Accordingly, the BVCA intends to meet with the major UK banks to see if we can jointly develop a protocol for restructuring situations in order to promote a rescue culture which will benefit both lenders and investors as well as saving businesses and jobs. No doubt the banks will also have their own suggestions as to how private equity firms can help to make the restructuring process more efficient.

We hope that the banks will be receptive to our initiative as mid-market private equity portfolio companies in aggregate represent a significant exposure for them and private equity houses actually have both the money and the will to fix their problem companies.

For more information on the survey, please email research@bvca.co.uk with Mid-Market Debt Survey in the Subject.

Research Team Note - The Private Equity Secondary Market

In the first of a series of commentary articles on topics pertinent to the private equity and venture capital industries, the secondary market is discussed and is available via the link below:

<http://www.bvca.co.uk/Research/Research-Notes>

The BVCA intends to meet with the major UK banks to develop a protocol for restructuring situations.


Publication of the quarter: Returns to Venture Capital January 2009, M. Wright and R. Chopraa

This highly useful and informative literature review of all papers on the performance of venture capital is a timely and much needed piece to dispel some of the myths around the industry.

The returns to private equity investment have become a vexed issue, attracting widespread debate in the media, government and among researchers. Much of the attention has focused on later stage buyout investments but there is a general move towards greater transparency and disclosure of the returns to both early and late stage venture capital investments. Shortcomings in the information provided to investors may mean that limited partners are restricted in their ability to judge the investment record of the VC funds in which they seek to invest. In this work, returns are examined at two levels. The literature on returns to venture capital is, unsurprisingly, mainly concentrated in finance and economics journals but a stream of studies has also appeared in entrepreneurship journals. Reviews of the literature relating to the different stages of the venture capital investment process, from deal sourcing through to exit, are available in Wright and Robbie (1998) and Wright, Sapienza and Busenitz, (2003). A segment of the main findings from the studies reviewed are highlighted below.

Examples of the Summary of Studies of Returns to Venture Capital

| Author | Sample Description | Data Sources | Method of Analysis | Summary of Findings |
|---------------------------|---|---|--|--|
| Gompers and Lerner (1999) | 419 US venture capital partnership agreements and offering memoranda for funds formed between 1978 and 1992 | Partnership agreements collected by 3 organisations: Aneneas Group, Kemper Financial Services and Venture Economics | Multivariate regression analysis, including Ordinary Least Square (OLS) analysis | Compensation of established funds is significantly more sensitive to performance and more variable than that of other funds. Older and larger funds have lower base compensation and performance and pay sensitivity do not appear to be related. |
| Dixon (1991) | 30 London-based specialist UK venture capital companies, all listed on Stop Hayward and represented approximately 20% of the total number of UK funds | Interviews with the executives constructed around a questionnaire | Mean scores, percentages of total sample mentioning it and standard deviations | The most important factor venture capitalists look for in a proposed investment is the experience of the management team, over the projected returns and turnover. The project's financing stage determines the risk premium, as the required rate of return is an arbitrary IRR to the proposal, not calculated through theoretical pricing models. |
| Wright and Robbie (1996) | 74 UK venture capital institutions listed as full time members of the BVCA | Mail questionnaires to chief executives of the venture capital firms or senior colleagues | Mean scores, standard deviations and Mann-Whitney U test of differences | Venture capitalists make greater use of discounted cash flow approaches and less use of asset-based methods, reflecting the use of IRRs as an important indicator of investment performance. They also use wide non-financial information to test the robustness of the accounting and financial projections. |
| Manigart et al. (1997) | 136 venture capital firms from UK, France, Netherlands and Belgium | Questionnaires filled by the senior managers of venture capital firms | Correlation analysis | The most widely valuation method in the UK is multiplication of past/future earnings with some price-earning ratio. In Netherlands and Belgium it is the discounting of future cash flows, and in France it is the book value of net worth. |

This publication is due to be released in: Wright, Mike, and Chopraa, Riva, 2009. "Returns to Venture Capital" in Douglas Cumming, ed., Companion to Venture Capital, Wiley Press, forthcoming. 

Recent publications

Private Equity Related

Corporate Governance and Value Creation: Evidence from Private Equity, January 2009, V. Acharya, M. Hahn and C. Kehoe

Deal-level data on private equity transactions in the UK initiated during the period 1996 to 2004 by mature private equity houses is examined and the authors un-lever the deal-level equity return and adjust for (un-levered) return to quoted peers to extract a measure of “alpha” or abnormal performance of the deal. The alpha is significantly positive on average and robust during sector downturns. In the cross-section of deals, higher alpha is related to greater improvement in EBITDA to sales ratio (margin) and greater growth in EBITDA multiple during the private phase, relative to that of quoted peers. In particular, deals with higher alpha either grow their margins more substantially, and/or grow multiples more substantially, whilst expanding their revenues only in line with the sector. Based on interviews with general partners involved with the deals, the authors find that deals with higher alpha and higher margin growth are associated with greater intensity of engagement of private equity houses during the early phase of the deal, employment of value-creation initiatives for productivity and organic growth, and complementing top management with external support. Overall, the results are consistent with mature private equity houses creating value for portfolio companies through active ownership and governance.

The European Venture Capital and Private Equity Country Attractiveness Index(es), November 2008, A. Groh, H. Liechtenstein, K. Lieser

The authors calculate composite indices to compare the attractiveness of 25 European countries for institutional investments into the Venture Capital and Private Equity asset class. To achieve this 42 different criteria were used, and an aggregation structure was proposed that allowed for benchmarking on more granulated levels. The United Kingdom leads the ranking, followed by Ireland, Denmark, Sweden, and Norway. The analysis revealed that while the UK is similar to the other European countries with respect to many criteria, there are two major differences which ultimately affect its attractiveness: its investor protection & corporate governance rules, and the size and liquidity of its capital market. The state of the capital market is likewise a proxy for the professionalism of the financial community, for deal flow and exit opportunities.

The Rise of Corporate Governance in Corporate Control Research, October 2008, J. Netter, A. Poulsen, M. Stegemoller

A review of the articles published in this Special Issue on Corporate Control, Mergers, and Acquisitions sees new evidence on several aspects of corporate control and governance including the value and performance effects of various ownership groups, the impact of internal governance structures, the effects of regulatory changes on specific industries and evidence on bidding strategies in takeovers. This analysis leads to the examination of the evolution of corporate control research, broadly defined. The analysis shows a movement in research from mergers and acquisitions to a broader analysis of corporate governance, especially internal governance features. The authors suggest that there is a trend toward an increase in the relative importance of internal governance compared to discipline from the market from corporate control. This trend reflects an important change over the past several decades in the means through which the market disciplines corporate behavior.

Bankruptcy Codes and Innovation, September 2008, V. Acharya and K. Subramanian

The study argues that when bankruptcy code is creditor-friendly, excessive liquidations cause levered firms to shun innovation, whereas by promoting continuation upon failure, a debtor friendly code induces greater innovation. The paper provides empirical support for this claim by employing patents as a proxy for innovation. Using time-series changes within a country and cross-country variation in creditor rights, the authors conclude that a creditor-friendly code leads to lower absolute level of innovation by firms as well as relatively lower innovation by firms in technologically innovative industries. When creditor rights are stronger, technologically innovative industries employ relatively less leverage and grow disproportionately slower.

Overall the results are consistent with mature private equity houses creating value through active ownership and governance.

Venture Capital Related

IT and Regional Development: Lessons From the Growth of the Software Industry in India, Ireland, Israel, Brazil and China, October 2008, A. Arora and A. Gambardella

During the 1990s the software industry grew at spectacular rates in some emerging economies, generating much interest in the question of how countries behind the technology frontier had been able to achieve substantial growth in a technology intensive industry. In this paper, the factors that explain the rise of the software industry in Brazil, China, India, Ireland and Israel are explored, highlighting both what is common and what is different across the five countries. It is found that Brazil and China have relied upon the domestic market, while India, Ireland and Israel, have grown through exports. Although all countries were marked by substantial investments in human capital, India, Ireland and Israel have seen a more limited role of sector specific public policies and a greater role for private entrepreneurship. Moreover, many traditional explanations of success in technology intensive industries, namely clusters and knowledge spillovers in clusters, R&D subsidies, and venture capital appear to have played a modest role at best. Instead, MNCs, openness, and entrepreneurship have been far more important.

Transferability of the Venture Capital Model to the Corporate Context: Implications for the Performance of Corporate Venture Units, September 2008, S. Hill, M. Maula, J. Birkinshaw, G. Murray

While recent literature has advocated the transfer of venture capital (VC) practices and structures to corporate venture (CV) units, the wisdom of this advice has not been subject to rigorous empirical scrutiny. The authors test the implications of the VC model for CV unit performance using a longitudinal database combining survey, archival and survival data on 95 CV units. VC model elements of high-powered incentives, autonomous organization, investment syndication, investment staging, and specialization were each associated with higher CV unit performance. Critically, different elements of the VC model predicted improvements in either strategic or financial performance in CV units. Survival of the CV unit was strongly associated with employing the VC model, partially mediated by enhanced performance.

Timing of International Market Entry of UK and German High-Tech Start-Ups, August 2008, G. Licht, G. Murray and M. Woywode

The paper examines the impact of technological product advantages, prior international experience of the management, firm size and age, country differences, and sunk costs as determinants of the timing of international market entry. The timing of internationalisation is analysed using 'event history analysis' for 600 British and German start-up companies in high-technology industries. The results indicate that the incidence of internationalisation increases over time. For the majority of new firms the question is not whether the firm will internationalise but when. The analyses indicated that a high commitment to R&D fosters rapid internationalisation. The involvement of founder managers who are internationally experienced increases the speed of foreign market activity. Working against rapid internationalisation was a high level of product customisation. The findings suggest that timing of internationalisation is a dynamic process which is influenced by initial human capital endowment, technological advantages, and learning from of day to day activities. 

Disclaimer

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For further information
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