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Fostering Dynamic Growth in New Ventures through Venture Capital: Conceptualizing Venture Capital Capabilities

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There is ample evidence of the influence of venture capital on the creation and growth of new ventures, yet scant attention has been paid to the heterogeneity of venture capitalists and their capacity to contribute to the dynamic growth of new ventures. This paper aims to contribute to the existing literature by exploring the notion that venture capitalists have beneficial effects on the growth of new ventures when they rely on a set of distinctive skills and processes that we associate with venture capital capabilities. We bridge the venture capital and resource-based view research streams to identify the foundational mechanisms of venture capital capabilities. We develop a set of propositions to test empirically and discuss the implications of our study for research and practice.

Introduction

The growth of new ventures is an enduring issue in management research. Since Penrose's (1959) study, scholars have been investigating the constraints that influence the growth of new ventures, such as the liabilities of newness or smallness (Carayannopoulos, 2009), with the aim to explain variance in growth rates across nascent firms (see Gilbert et al., 2006 for a review). Interest in the growth of new ventures is not confined to the academic domain. The business press is filled with stories of charismatic and visionary founders who transform business ideas into successful business models. These stories generally depict a venture capitalist standing beside entrepreneurs (Florin, 2005; Zider, 1998). However, the capabilities that venture capitalists provide in facilitating new venture growth remains unclear.

Venture capitalists are conventionally depicted as providing new ventures with funds that more traditional channels, such as banks, are unlikely to grant given a new venture's lack of hard assets for securing debt. However, it has been increasingly recognized that venture capitalists play a strategic role in helping new ventures move from an entrepreneurial to a professionally-managed state (Zider, 1998). As a result, the influence of venture capitalists transcend the single firms and assures the competitiveness of entire ecosystems.[1] For example, venture capitalists promote breakthrough innovation (Ferrary and Granovetter, 2009). At the ecosystem level, venture capitalists serve as one of the more effective systems for indirect selection of new ventures, and they shape the environment where new ventures evolve (Baum and Silverman, 2004). At the firm level of analysis, venture capitalists influence the development of the ventures in which they invest through a combination of sorting/scouting effects and treatment/coaching effects (Bertoni et al., 2011). This has led to the observation that venture-backed companies have been found to outperform non-backed counterparts (Bertoni et al., 2013).

Literature has begun to explore the reasons behind the performance benefit of venture capitalists. Existing research about venture capital provides evidence that venture capitalists learn from repeated experiences to refine their abilities to scout and coach promising ventures (e.g., Petty and Gruber, 2011). Research also highlights that venture capitalists endow the ventures that they back with capabilities (Arthurs and Busenitz, 2006). Building on and extending these findings, we advance the idea that scouting and coaching activities may represent distinctive venture capitalists' capabilities, which allow them to create and capture value from the companies they back and to obtain competitive advantage vis-à-vis other venture capitalists.

If true, differences in venture capital capabilities can help to explain heterogeneities across the growth rates of venture-backed companies and across venture capitalists' performance because these capabilities affect the causal mechanisms (i.e.,

[1] Moore (1996, p. 26) defines a business ecosystem as "an economic community supported by a foundation of interacting organizations and individuals. This economic community produces goods and services of value to customers, who are themselves members of the ecosystem. The member organisms also include suppliers, lead producers, competitors, and other stakeholders." The concept of an ecosystem is broader than that of an industry or geographical cluster and includes both competitive and cooperative dynamics among the different actors of business life.

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