University of Navarra

Working Paper
WP-180
March, 1990

EUROPEAN VENTURE CAPITAL: STRATEGIES AND CHALLENGES IN THE 1990s

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EUROPEAN VENTURE CAPITAL: STRATEGIES AND CHALLENGES IN THE 1990s

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Abstract

This paper summarizes the current perceptions of leading European venture capitalists as an aid to those involved in formulating strategies or determining public policy. Secondarily, it provides an excellent view of venture capital in the 1990s against which actual developments may be compared. These views are developed in a survey of 34 firms, which manage over one-quarter of the European venture capital pool.

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EUROPEAN VENTURE CAPITAL:
STRATEGIES AND CHALLENGES IN THE 1990s*

Introduction

In a study of the European venture capital industry during the early 1980s, Tyebjee and Vickery (1988) concluded that "Venture capital is as yet in its infancy in Western Europe... the investment activity manifested by European venture capitalists has been relatively small." They noted that European venture capitalists invested about one-eighth as much as their U.S. counterparts over the four years from 1981-1984. Even after allowing for the different sizes of the economies, the figures were only slightly less dramatic; viewed as a fraction of gross domestic product, European investment was about 22% of U.S. levels.

A few years later, the situation had changed dramatically. In 1988 European venture capitalists invested more than their U.S. counterparts for the first time – more in absolute amount and as a fraction of gross domestic product. They also raised more funds for future investment than did U.S. venture capitalists.

Clearly European venture capital has "come of age" since the late 1980s. Even so, each venture capitalist faces issues which will profoundly influence strategies for the 1990s. Such issues include the industry's growth prospects, trends in competition and rates of return, as well as the coming single European market in 1992.

Porter in *"Competitive Strategy"* (1980, chapter 3) speaks of the importance of understanding how an industry's participants view themselves and their industry. Such knowledge becomes an important component in choices about expansion, industry focus, personnel selection, international vs. domestic emphasis, and a host of other issues.

This study summarizes the current perceptions of leading European venture capitalists as an aid to those involved in formulating strategies or determining public policy. Secondarily, it provides an ex ante view of venture capital in the 1990s against which actual developments may be compared. These views are developed in a survey of 34 firms, which manage over one-quarter of the European venture capital pool.

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* The authors gratefully acknowledge the financial support of the Chair Fundación Bertrán de Iniciativa Empresarial at IESE and the collaboration of European Venture Capital Association, EVCA.

Using a questionnaire and a direct interview, we cover four general subjects:

- Fundraising by venture capital firms.
- Investments of venture capital firms.
- The environment for venture capital investing in Europe.
- Competition and evolving strategies within the venture capital industry.

The first three deal with the forces which constrain venture capital strategies, and the fourth with the strategies themselves.

Background

Venture capitalists, particularly in the United States, have received considerable attention from United States researchers, with much attention being given to how venture capitalists do their jobs. Tyebjee and Bruno (1984) noted that all venture capitalists must perform five functions: raising funds, originating (or finding) investment opportunities, screening opportunities, structuring investments, and supporting existing investments. The questionnaire for this study deals with each of the five areas, emphasizing the trends in each.

Venture capitalists pride themselves on judging the quality of a company's strategy. In at least one case they have been asked to articulate and evaluate their own strategies. Robinson (1987) surveyed 53 United States' venture capital funds in the mid-1980s, and found widespread similarity in goals, sources of funds, and methods for evaluating prospective investments. Respondents also agreed on the main directions for the overall industry:

- It would face increasing competition from other financing sources, and would see a decline in the rates of return being earned.
- The average firm would increase in size, as would its average investment.
- Individual venture capital firms would provide greater assistance to their investees and would devote more effort toward promoting their particular skills.

On the whole, respondents believed a period of scarcity had ended. One would no longer earn high returns simply by following industry norms- "a 'uniform model' is most likely out-of-date" (Robinson, 1987, p. 74).[1] Although the time seemed right for new strategies to emerge, Robinson found "the overall characterization of these firms' strategies is one of uncertainty and reaction" (p. 73). He concluded that such uncertainties reflected the early phase of a restructuring into multiple segments such as industry specialists, start-up specialists, and large, later-stage investors.

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[1] Robinson uses the "uniform model" as a convenient starting point, but does not claim that it truly existed in venture capital. In a recent history of venture capital, Reiner (1989) provides evidence that investment strategies of venture capitalists in the 20 years following 1945 were relatively uniform. They were looking for young companies with proprietary technologies in growing markets. However, many other aspects of their strategies were not at all uniform, including fundraising, internal organization, legal form, sources of investments, syndication practices and investment instruments. The increasing dominance in the United States during the 1980s of independent limited partnerships with institutional investors has created greater uniformity in many aspects of venture capital strategy even as it increased the variation in investment strategies.

Paralleling Robinson's approach, this study will examine whether European venture capitalists have followed a "uniform" strategy to date, and whether practitioners feel their traditional strategies will remain appropriate.

Tyebjee and Vickery's (1988) study of European venture capital in the early 1980's focused principally on the state of the industry, and the underlying environments for new companies. They noted that the countries within the European Community exhibited "considerable differences in the technology, tax and economic policies... in addition to cultural and linguistic diversity" (p. 126). Their data showed dramatic variations in the amount of venture capital investment among the European countries.

Table 1, which updates their data for the seven European countries with the largest "pools" of venture capital, shows that at least five patterns exist today:

- The United Kingdom is experiencing a venture capital "boom." Investment has grown rapidly, and as a fraction of domestic product is nearly five times that of its closest followers.
- France and Belgium are in a period of high growth, and have reached a level of activity matching that of the United States.
- The Netherlands is relatively mature; growth is the lowest of the group, but the activity level remains fairly high.
- Italy and Spain have "taken off." From very low levels of investment in the early 1980s, they have moved to activity levels about one-half that of the United States.
- Germany remains at a "pre-takeoff" state. Activity levels, relative to domestic product are by far the lowest of the group.

Table 1

Venture Capital Activity in Western Europe

	1981-1984 (Average)[1]		1988[2]		
	Investment (ECU Million)	Activity Index[3]	Investment (ECU Million)	Activity Index	Growth
Belgium	9	14	75	92	733%
France	23	6	667	136	2800%
Germany	22	5	125	12	468%
Italy	3	2	122	40	3966%
Netherlands	48	48	85	137	77%
Spain	n/a	n/a	91	60	n/a
U.K.	257	75	2,497	632	871%
Total	362	24	3,662	162	911%
U.S.A.	2,992	100	2,553	100	-15%

Notes:

1. Source: Tyebjee and Vickery (1988).
2. Source: EVCA (1989).
3. Activity index is Investment/GDP. It is normalized such the index for the United States is 100.

The rapid growth of the industry during the late 1980s would probably surprise Tyebjee and Vickery, but their analysis correctly identified the trends in individual countries. For example, they viewed the United Kingdom – with its combination of tax incentives, an active second market, and a cultural tradition reasonably favorable toward entrepreneurs – as the most favorably situated among the European countries. They also noted that the introduction of important tax incentives and the initiation of a second market in France were important precursors of growth in venture capital. Germany, despite a cultural tradition reasonably conducive to entrepreneurship, had an unfavorable tax structure, and offered poor opportunities for exit via public offering or acquisition. Thus they were less optimistic about the growth of venture capital there.

The success of venture capital in Italy and Spain might also surprise Tyebjee and Vickery. The tax structures remain unattractive, and the avenues for exiting from a successful investment are limited. One objective of this study will be to understand the growth in those two countries; presumably they reflect forces not previously identified.

Methodology

Based on a review of prior studies, as summarized above in the Background section, we developed a questionnaire and interview. Rather than cover all the activities of venture capitalists that Tyebjee and Bruno (1984) discuss, we focused on the four areas where substantial variation exists. As noted in the Introduction, these include sources of funds, how the funds are invested, developments within the environments of the host countries, and competitive and strategic developments within the venture capital industry. Relatively little attention was given to objectives and methods for evaluating opportunities, because all prior studies have found these to be relatively uniform.

The questionnaire uses a combination of short answers and multiple choice responses.[2] It is designed to allow wide latitude in answering, which means it is not suitable for statistical analysis. Accordingly, this study analyzes the responses in an informal, qualitative manner.

The staff of the European Venture Capital Association (EVCA) assisted in the selection of a sample. Attention was given to obtaining coverage of each of the seven largest venture capital markets with representation by all types of firms – independent, bank related and government related. The firms in the sample embody four investment strategies: technology specialists; large, broad funds with significant transnational investments; late stage investors; and local generalists. The type of firm and investment strategy are somewhat related; the bank and government funds tended to be late investors or local generalists while the independent funds dominate the other two categories. Table 2 summarizes the characteristics of the sample.

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[2] A copy of the questionnaire and a compilation of results is available from the first author.

Table 2

Sample Characteristics

	Number		Cap. Managed/ Total for Country	Type of Firm			Investment Strategy			
	Sent	Replied		Indep	Bank Sub.	Gov't	Large Broad	Technical Specialist	Local Generalist	Late Stage
Belgium	7	5	41%	4	0	1	1	0	3	1
France	7	6	13%	4	2	0	3	1	1	1
Germany	4	3	24%	3	0	0	0	2	1	0
Italy	4	3	42%	3	0	0	0	1	1	1
Netherlands	7	3	25%	1	2	0	0	0	1	2
Spain	5	5	43%	2	2	1	0	0	4	1
U.K.	9	9	26%	7	2	0	5	1	2	1
Total	43	34	25%	24	8	2	9	5	13	7

The 34 respondents manage ECU 4.3 billion, about a quarter of the European venture capital pool. They comprise 8% of Europe's 427 venture capital firms, and about 26% of the EVCA's 132 members. With an average of ECU 125 million under management, they are about four times as large as the average of the remaining 393 funds. All participants are viewed as leading funds in their respective countries, and are generally among the older funds. However, ages vary widely depending on the age of the venture capital industry in a country. Despite the large average size, ten funds from five countries have less than ECU 30 million under management, and provide representation by smaller venture capitalists.

Table 2 shows that European venture capital has already evolved beyond a "uniform model," which Robinson (1987) posited as the industry's starting point. It has at least four groups with distinctive investment strategies. These roughly parallel the structure in the United States, although U.S. firms as a group are much more focused on technology-based companies. Thus the counterpart of the European technology specialist is an industry specialist, which emphasizes medical products or software, for example. The United States has two other specialized groups: seed and start-up funds, and consumer funds (a field covered in Europe by generalists). With its shorter history, European venture capital may have developed fewer specialties, but multiple investment strategies clearly exist with the most active countries showing the greatest variety.

Findings: Sources of Funds

Table 3 shows the expected changes in funding sources for each country. Sources which have traditionally been important are noted with an asterisk (*). Pension funds and insurance companies are clearly expected to expand their roles beyond the United Kingdom and The Netherlands, where they are currently important sources. In most countries, some respondents expect a decline in one or more of their traditional sources; however, such opinions are scattered when compared to the strong agreement about pension funds.

Table 3

Trends in Sources of Funds (% reporting)

	Belgium	France	Germany	Italy	Netherlands	U.K.	Spain	Total
Replies	-4	-6	-2	-2	-3	-7	-5	-29
Increasing								
Pension Funds	50	67	100	50	67	*57	100	69
Insurance	50	50	100	50	67		80	*48
Corporations	50		50	50	33	29	*40	31
Banks	*50	*50			*67	*29	*33	*37
Individuals					33	14		7
Local Authorities						14		3
Stock Market	25							3
Decreasing								
Government		33	50				*40	17
Banks		33	*50				*40	*17
Corporations		*50	50					14
Individuals		17				14		7
Pension Funds					33			*3
Insurance					33			*3
Stock Market		17						3

Note: Five captive firms did not respond.

Table 3 suggests that independent venture capital firms, which raise funds from pension funds, insurance companies, and corporations, may grow vis-à-vis the bank or government related firms. This would follow the pattern of the United States.

The amount that venture capitalists can raise determines their investment level, so trends in the availability of funds are important to every venture capitalist. By a 70-30 margin, the respondents expect continuing growth over the next few years. The responses vary by country, with Dutch venture capitalists forecasting a decline in future commitments, and with a 50-50 split among French and Italian venture capitalists. Everyone realizes that the past growth will not continue indefinitely, but most feel that the industry is still relatively immature.

Also by a 70-30 margin the respondents envision more funds coming from outside their countries. Historically, about 80% of funds have been raised domestically, with another 10% from other European countries. In the future other European countries, the United States and the Far East are expected to have approximately equal importance. The perceived motive of the outside investors is geographic diversification. If this proves true, it may favor large, established firms, which tend to be better known internationally and are more diversified than the more specialized firms.

In principle, a large institutional investor could integrate forward into venture capital, but most respondents are unconcerned about this source of potential competition. They note that institutions particularly value their skills at assisting investees, along with their abilities to locate entrepreneurial investments and negotiate special investment arrangements. These, as opposed to size, diversification and general financial contacts, are the qualities which institutional investors would find the hardest to acquire. Supporting an overall feeling of security, several respondents state that government programs, wealthy individuals, and corporate venture departments have all proven to be poor substitutes for venture capital.

In summary, the venture capitalists surveyed expect further growth in the pool of venture capital. They expect changes in the sources of funds with increasing investment from relatively passive sources such as pension funds and overseas investors, a trend which may favor large, independent funds.

Findings: The Market for Investments

Venture capital firms exist to make investments in sectors offering unusually attractive returns, so the questionnaire asked whether today's returns are as good as they have been, and what changes are occurring in the relative attractiveness of certain industries, and types of companies (e.g. start-ups, expanding firms, management buy outs).

Table 4 summarizes the overall rates of return – historic, as well as expected returns for the respondent's firm and for the industry. No obvious variations exist across countries. With the caveat that few funds reported their historical returns, Table 4 indicates that returns have been attractive and that the industry participants expect them to remain so, although the trend will be downward. Many who did not provide a forecast say they had no idea what future returns will be, but that they would be lower on the average than they have been. Two additional questions about competition among venture capital firms elicited near unanimity that it will increase.

Table 4

Rates of Return on Venture Capital Investments (% per year)

	# Reporting	Low	High	Average
Firm's past return	8	0	45	21
Firm's expected return	25	12	40	26
Industry's expected return	23	8	30	18

Of the 21 firms which provide a forecast of the industry's and firm's performance, 15 feel their firms will perform above the industry average, and only two expect it to perform below it. This is consistent with similar surveys in the United States. These optimistic assessments may have three sources, each with important implications:

- They may reflect the benefits of being a leading fund. That is, leading funds, regardless of location, will enjoy above-average returns. If true, the implications for investors, for potential new entrants, and for the funds is obvious.
- They may reflect unrealistically high expectations. If true, this may be communicated to investors and lead to unrealistic expectations on their parts and to unwarranted expansion. This may in turn cause low returns, disappointments and a subsequent shrinkage of the venture capital pool.
- They may be simple expressions of self-confidence by each firm, an attitude which places the burden for regulating the flow of funds totally on the prospective investors

in venture capital. That is, the separate venture capital funds may be efficient allocators of the pool which is available, but they may not be good judges of the optimum size of the pool.

If the forecasts of overall returns indicate an expectation of "business (almost) as usual," that expectation does not carry over regarding which industries to invest in. For Europe as a whole, the electronic industries received the most investment in 1988 – almost a quarter of the total. They are followed by consumer products and services with 18%, and general manufacturing with 12%. With respect to electronics and manufacturing, the respondents expect a decline in future years.

Our survey asked for opinions about "attractive" and "unattractive" industries over the next few years. An industry could appear in both categories if respondents disagree about attractiveness, or if conditions vary among countries. However, there is a strong consistency. Industries which many people rank as attractive find only a few who rank them unattractive, and vice versa. The electronic industries (with the exception of software) are viewed as the least attractive sector over the next few years.

Regarding attractive sectors, the leading response by far is "any sector." During the interviews, the venture capitalists explained that, regardless of industry, they believe the unification of markets in 1992 will create opportunities for companies that enjoy strong positions today in their home countries. After 1992, such companies should be able to grow rapidly at the expense of weaker firms in other countries, firms that previously were sheltered from transnational competition.

Other sectors scoring high in "attractiveness" include consumer goods and services, bio/medical products, software and communications. The breadth of this list reflects an important difference between Europe and the United States, where electronic and biomedical investments have received nearly 70% of the total amount invested. The broader investment pattern in Europe may imply an ability to sustain a higher level of venture capital investment relative to gross domestic product without depressing returns.

Supporting the view that strong companies in any sector will benefit from the unification of markets, respondents in every country expect a continuing increase in buyouts because of the attractive returns. Buyouts currently represent one-sixth of the transactions and receive 37% of total venture capital investment. Start-ups and early stage financings, which were 28% of the transactions in 1988 and received 13% of the funds, are not anticipated to grow. This is probably consistent with a de-emphasis of electronic firms, and a growing interest in companies that will benefit from the unification of markets in 1992.

A potential risk of backing "national champions," who are expected to thrive in the post-1992 environment, is that each country's venture capitalists will expect to gain at the expense of the other countries – a modern variation of "mercantilism." Such expectations may be based on limited knowledge of the competition, given the tradition of investing almost all one's funds domestically (90% of venture capital funds were invested domestically in 1988). This pattern of investing close to home is found in the United States as well, and derives from the advantages of close contact between venture capitalist and investee after the investment is made. In any case, it poses a challenge whether most venture capitalists, and whether venture capital as currently practiced, will be well suited for guiding strong national firms into the arena of transnational competition.

As a rejoinder to the above concern, nearly every respondent expects to become active as an investor in other countries. Most expect to be primarily investing in the closest neighboring country. Thus British, Belgian and German firms expect to be much more active in France. French firms expect to become more active in Italy and Spain. Spanish firms expect to invest in Portugal. Only The Netherlands, which emphasizes Spain and Portugal, deviates from the pattern.

Further supporting a planned increase in transnational activity, many respondents note that they will use their international connections more actively in future investments. Such an increase in transnational investing, if it occurs, will depart from a "tradition" in which only a tenth of the transactions are syndicated transnational. Venture capital syndicates of any kind are less common in Europe than in the United States. Conceivably the need to guide investees in the post-1992 environment may provide the impetus for greater syndication. If so, it will probably enhance the position of the firms in our sample, starting with EVCA members, who have already developed international connections even though they have not utilized them heavily.

Findings: The Environment for Venture Capital Investing

The above subjects, sources of funds and the investment of funds are at the heart of venture capital. Three peripheral influences were studied as well: the determinants and status of the "climate" for venture capital, the expected effects of the single European market, and the effects of "high tech zones."

Not surprisingly, the survey shows broad agreement among venture capitalists on the need for tax incentives and active public stock markets for young companies. However, our respondents rank a third quality, a "good entrepreneurial climate," at least as high as the first two. By this they refer to public acceptance of entrepreneurship, job mobility, favorable attitudes by banks toward young companies, science parks, and the like. As a group venture capitalists have been active in communicating the need for tax incentives and public markets, but the promotion of entrepreneurship has received less emphasis. As the first two are accomplished, the venture capital community may devote greater attention in the future to the entrepreneurial climate.

The respondents, regardless of country, agree that Britain and France meet the three conditions the best, with The Netherlands a distant third. They also agree that the remaining four countries do not yet provide the conditions for a healthy venture capital industry, with Germany being the laggard.

To date, the European Economic Community is perceived as having little influence on the climate for venture capital, which many regard as appropriate; no one views it as a harmful force. Looking to the single European market in 1992, respondents agree unanimously (with one abstention) that it will be a positive force. Many believe it will lead to increased competition among venture capitalists, but this will be offset by the creation of many investment opportunities and a much improved second market system.

Several respondents feel the single European market will lead to greater uniformity in public policies toward venture capital. For example, transnational expansion by venture capital backed companies in the two most active countries, France and the United Kingdom, will increase the pressures on the other four governments to improve their venture capital environments. The effect could be substantial. If the four increased their investment rate (as a fraction of domestic product) only to that of the United States, total European venture capital activity would grow by ECU 790 million, a 23% gain.

If the single European market produces opportunities for companies to expand transnationally, the venture capital industry is not yet structured to support it. Most funds emphasize domestic investments, and do not routinely syndicate their investments. Only about a tenth of the investments are syndicated transnationally. This means that most funds have limited direct experience with the cultural, fiscal and legal environments of the other European countries. However, our respondents feel that as the needs arise, they will form transnational syndicates, and such syndicates will be effective vehicles for guiding companies in international competition.

What remains to be tested is whether the formation of transnational syndicates is as easy as our respondents suggest. One might expect a rapid growth in such syndicates over the next year for two reasons. First, venture capitalists will be cementing their relationships with the funds they plan to work with in future years. Second, if opportunities for building from a domestic to a transnational base are common, investors will become involved prior to 1992 in order to get an early start.

One frequently mentioned device for building technology-based industries is the creation of "high tech" zones. We asked whether and where such zones would emerge. With the exception of the United Kingdom's venture capitalists, who are doubtful about "high tech" zones, about two-thirds of the respondents expect them to play growing roles in the future. This question, more than any other, generated strong differences. Most of the British respondents view them as "irrelevant," whereas many others think they are "a must for start-ups" and have "very high potential." But there is little agreement where such zones would occur. Several mention the need to be where the right people and infrastructure are; some suggest being near a good university; many mention specific countries with France being the leader. Very few name their own country as leading candidates for "high tech" zones. Several say they have no idea where such zones will emerge, but they will be important.

Of the three environmental questions, "high tech" zones are the only one on which opinions vary widely. The reason may be that venture capitalists have not thought carefully about them because they will develop slowly and they are not very important to the future of the venture capital industry. Technology-based companies are the largest recipients of European venture capital; however, their role is far less central than in the United States. For example, electronic, medical and biotechnology companies receive one-third of European venture capital but 70% of U.S. venture capital. Except for the five technology specialists, our respondents invest in many industries and are not counting on an explosion in technology based firms.

Findings: Competition Among Venture Capital Firms

When asked if they expect growing competition within the industry, over 85% say "yes." Those who say "no" feel that a shakeout is imminent that will eliminate many participants – and then competition will diminish. In combination, these point to near unanimity that competition among venture capital firms will create future difficulties. These responses conflict somewhat with their forecasts of future returns, which do not show any pronounced declines and with the feeling that the pool of funds will continue its steady growth. The explanation may be that competition will not be based on price, leaving overall returns unaffected by competition. Alternatively, the response may differ depending on how the question is asked.

Two questions deal with each firm's planned response if competition becomes stiffer. Two firms stated that such information is proprietary, but all others provided responses. The most common view is that the firm will continue to thrive by being "better" (e.g. having better managers, better quality, a better reputation) than its competitors.

The obvious question for those who differentiate themselves by being "better" is whether that difference can be perceived in advance by the providers of funds and by entrepreneurs. A few responses mention plans to develop a communication or public relations program, but most do not discuss how they will communicate their advantages.

The five respondents, who are technology specialists, and the nine, who are large, internationally oriented investors, feel their investment strategies will help them in an era of growing competition. The other two groups, local generalists and late stage investors, feel their strong national reputations will be attractive to transnational syndicates because they will provide local knowledge of marketing, business practices, and management resources. In principle, all four groups could be right. They are not necessarily direct competitors.

The survey asked each firm to identify its current strengths and the areas it planned to strengthen. The questionnaire identified the five functions[3] discussed by Tyebjee and Bruno (1984) and asked for comments. Table 5 shows the results. Among current strengths, screening and analysis of opportunities clearly ranks highest. Exiting ranks the lowest and other four are nearly even. The responses are generally the same across the seven countries. Including comments, the replies identify an average of 2.60 strengths, indicating that most do not believe they are uniformly strong on all the functions of venture capital.

Table 5

Present and Planned Functional Strengths of Venture Capital Funds (% reporting)

	Present	Planned	Increase
Raising Funds	34	50	16
Originating Investments	47	66	19
Evaluating Opportunities	72	78	6
Structuring Investments	41	50	9
Assisting Companies	47	53	6
Exiting	12	22	10
Other Strengths Reported			
International Network	16		
Corporate Shareholder	3		
Bank Subsidiary	3		
Track Record	3		

Note: Percentages are based on 32 replies.

[3] Support of investments was divided into direct assistance and "harvesting" (or exiting), making a total of six possible replies.

Taking account of their planned improvements, origination becomes nearly as strong as evaluation, with fundraising also gaining substantially. The effect is to produce a greater balance in a fund's capabilities. Although a movement toward balance could be a strategy shift in response to changing competition, in this case it appears to reflect the natural development of a fund. The younger and the smaller funds are currently less balanced and are planning to become more balanced. The older, larger funds generally feel they are strong in most areas, and do not plan many changes.

On the whole, the survey produces little evidence that firms are concerned about their present strategies or are planning important shifts. The impression is one of an industry which has grown smoothly, and expects a gradual increase in competition, but not a change that will threaten the existing participants.

Discussion

The rapid growth of venture capital in Spain and Italy to levels much higher than in Germany (as a fraction of GDP) remains puzzling. Nothing in the responses reveals differences in attitudes or strategies among the three countries, and there is general agreement that all three have unfavorable climates for venture capital. One plausible speculation is the Spain and Italy are less mature economies characterized by more shifts in industrial structure, and therefore creating more opportunities for venture capital.

Aside from that puzzle, the results of the survey are fairly clear. Venture capital has thrived when industries were young or in transition – situations in which incumbent competitors or powerful potential entrants often respond slowly and inappropriately. In Europe these opportunities have not followed the United States' pattern of being heavily concentrated in technology industries, and European venture capitalists have built a strong industry by investing in many types of companies. To be more precise, we should return to the patterns discussed in the beginning. Belgium, France, The Netherlands, and the United Kingdom have built strong venture capital industries. Italy and Spain are moving rapidly after a late start. Germany is lagging. Seven countries with seven sets of public policies, traditions and infrastructures have provided seven interesting "experiments." Some have done better than others, but the overall results are impressive.

The unification of European markets in 1992 promises to be another transition that will create many opportunities for venture capitalists. But the opportunities will involve transnational expansion, and one may doubt whether the traditional domestic focus of most venture capitalists has prepared them for such investments. The responses in our survey suggest that venture capitalists feel otherwise. They are aware of the opportunities, and expect to benefit from them. However, regardless of country, they seem to feel well prepared to deal with the coming opportunities. They may strengthen a few weak spots and participate in more transnational syndicates, but generally it will be business as usual, perhaps with slightly more competition and slightly lower rates of return.

This response of "business (almost) as usual" is not inevitable. Options exist. For example, a large venture capital fund could establish offices in other countries, or it could establish financial ties with existing firms. It could build a network of small investor/partners with special knowledge in promising countries and industries, or in important functions such as recruiting, public relations or information systems. It could raise funds from prestigious investors in other countries in order to increase its prominence and credibility there. It could immediately increase the number of transnational syndicates it forms in order to accelerate the mutual learning required for separate firms to function effectively together.

A smaller fund could attempt to build a network of similar funds in several countries, which might include cross investment or even mergers. It could establish linkages to local universities or research institutes. If it were in a country with a poor venture capital outlook, it could develop local marketing expertise which it would use as a lever to join investment syndicates of companies hoping to expand into its territory.

The aforementioned strategies have all been tried with some success in the United States. Our survey respondents, as leading firms in their countries, and active members of the EVCA, are undoubtedly aware of these and other options available to them. Yet, with the exception of one firm which plans to add a merger and acquisition specialist to its staff, none of them went beyond the ideas of improving their functional balance and building their international connections.

Perhaps the answer is that venture capitalists regard such ideas as confidential. Or, as leading firms with international reputations, they probably will prosper in any case, and have little reason to experiment with strategic changes. They can leave the experimentation to new firms, who need novel approaches in order to enter the now established venture capital industry. The reputation of an established venture capital firm is a valuable intangible asset, which unsuccessful experiments may jeopardize. On the other hand, a successful experiment is easily copied. No patents or other barriers to imitation exist. Our respondents can simply adopt those innovations which prove successful.

In a different vein, instead of concentrating on how to beat the industry's average performance, an industry leader could propose cooperative programs to improve the overall average. Such programs would involve raising awareness of entrepreneurship, publicizing successful investments, sponsoring special purpose funds to invest in young, public companies, working with governments to improve incentives and so forth.

In the long term such measures would attract additional entrants to venture capital, and returns would be drop to levels which fit with the capital markets as a whole. However, the long term equilibrium might be far in the future. Total venture capital investment in Europe each year is still less than the capital and R&D budgets of a single electronic, chemical or pharmaceutical giant. European venture capitalists have already successfully pushed beyond the limits of the older United States' venture capital industry. The eventual scope of may be much broader.

Summary

The responses are interesting in what was said and what was not. A clear majority agree regarding sources of funds, industry growth and future investments. They expect the industry's growth to continue, with further increases in support from pension funds and insurance companies, and continuing declines in support from governments. They expect competition to increase among venture capital firms, producing moderate decline in rates of return. Investments will continue its shift away from early stage technology-based companies toward established companies that can benefit from the single European market in 1992.

Respondents left unstated the steps they would take to shift from domestic, non-syndicated investments to transnational investments. Implicitly they may feel the change will be a minor one. Additionally, no one discussed possible actions that could increase the overall demand for venture capital; their plans are intended to improve their individual positions.

With this forecast from its participants, it will be interesting to watch the evolution of the European venture capital industry during the next few years.

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