

Venture Capital and Exporting – Some Evidence from EU Countries¹

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Abstract

Purpose: The aim of this article is to present the results of the research on the export of venture capital backed firms in the European Union countries.

Methodology: For the purpose of this article, the author created four linear regression models. He decided for export revenue to be a dependent variable. Then, the author verified the influence of four independent variables on export value.

Findings: The research found that the turnover of venture capital backed firms positively influences their export value. Moreover, the costs of employees also play an important role in export value explanation. Nevertheless, the empirical study did not confirm any strong positive correlation of analyzed firms' export value with the number of employees and their share of shareholders' funds in operating income.

Limitations: The analyzed period was limited only to 2016. Second, the study used only one dependent and four independent variables. Further research must include other variables, especially moderating ones, such as entrepreneurship ratio or availability of external financing forms. Third, the regression models were based on data retrieved from Orbis Database and can induce uncertainty regarding its credibility.

Originality: At present, there are still only few research studies that explore the export of venture capital backed firms.

Keywords: export, internationalization, international trade, venture capital, financing

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Introduction

Scholarship considers venture capital (VC) funds to be an innovative source of financing for small and medium-sized enterprises (SMEs), mainly those in the seed and startup stage. The main point of these funds is to provide the firm with capital in exchange for shares. Additionally, the subject which invests in a given venture actively participates in the ongoing development of the financed firm ((Clercq and Manigart, 2007; Cumming and MacIntosh, 2003; Metrick and Yasuda, 2011). After a certain period of time, the fund withdraws the capital committed and, thus, realizes its profit or loss from the venture. Despite the prevalence of this investment scheme, there is a relatively small amount of research that considers venture capital backed firms' internationalization.

The research problem of this article concerns the impact of venture capital funds on the development of businesses' exporting in the EU countries. The aim of this article is to present the results of the research on the export of venture capital backed firms in the European Union countries. The author selected six countries mainly due to data availability: France, United Kingdom, Germany, Ireland, Slovenia, and Estonia. Moreover, this paper describes an early stage of ongoing research.

The theoretical part of this article discusses the essence of venture capital as a form of financing and refers to research on the internationalization of firms financed by these funds. The empirical part stems from the data obtained from Orbis-Bureau van Dijk and shows four regression models created to check whether the four designated independent variables – operating revenue, cost of employees, number of employees, shareholders' share in a firm's funds – impact export value.

Venture Capital as a Form of Financing

The demand for capital to finance innovative undertakings first appeared at the beginning of the twentieth century. At that time, the demand for this type of financing was related to the ongoing industrial revolution in Western Europe and the United States of America (Gompers, Lerner, 2001). As firms faced numerous financial problems, entrepreneurs sought alternative (external) sources of financing. Despite globalization, which enables venture capitalists to invest abroad relatively easily, scholars still consider venture capital to be a geographically-bound local market (Bruton et al., 2005). Currently, private equity capital quickly gains popularity among new ventures and instant exporters (Kazlauskaitė et al., 2015).

One finds many definitions of venture capital in a selective literature review. Tamowicz (1995) considers venture capital funds to be medium- and long-term capital, mainly invested in various types of equity securities (ownership) or quasi-equity (companies not listed on the stock exchange) to sell them at a higher price. Generally speaking, one may say that the capital injected into a firm has the nature of an equity share but not credit (debt), which simultaneously makes the firm's financing subject its co-owner (Tamowicz, 2004).

Aizenman and Kendall (2012) describe venture capital like Tamowicz (1995) but argue that VC mainly invests in private firms with high potential for growth. Prowse (1998) links venture capital with financing equity of small innovative enterprises (startups), which have a considerably greater potential from the very beginning of their activity (mainly in the early stage of the firm's development). This view agrees with Murray's study (1994) who states that venture capital funds are particularly interested in high-growth firms – often at the seed or startup stage – thereby it is difficult to obtain reliable information on their activities. Azarmi (2016) and Wright, Lockett et al. (2002) present the same perception as Murray. Bannock and Doran (1991) argue that venture capital is the main source of financing for small and medium-sized enterprises.

A very general definition of venture capital fund is proposed by EVCA:³ venture capital is a subset of private equity that refers to equity investments that mainly finance ventures related to startup, development, or expansion of an enterprise (EVCA, 2007; 2017).

The great evolution of research on venture capital funds occurred at the turn of the twentieth and twenty-first century. In that vein, Bergemann and Hege (1998) call venture capital the main source of startups funding. In many countries and especially in the United States, VC finances activities at the frontier of science and knowledge. Due to their innovative nature, venture capital projects inherently have a high risk of failure. Hellmann (1998) claims that, in comparison to traditional forms of financing, venture capital shows the following features: (i) support in project management through assistance in strategy building, technical support, consulting, and hire of key personnel; (ii) impact on the composition of firm's management board; and, (iii) the lack of protection for entrepreneur in the event of capital withdrawal from a venture.

³ The European Venture Capital Association (EVCA) was founded in 1983 and is located in Brussels. EVCA represents the concerns of the European private equity sector by, among others, standard setting and researching the wider private equity sector (including venture capital). In 2015, the organization changed its name to Invest Europe.

Several years later, empirical studies by Hellmann and Puri (2002) showed that companies financed by venture capital are more susceptible to staff changes than those without VC investment. According to these researchers, the founders of venture capital backed firms are pushed into the background, but the role of managing directors is overtaken by people from outside the firm; often directly linked to the venture capital funds that have invested in a given firm. According to Wach (2005), attracting venture capital investments depends on a stable group of small and medium-sized enterprises (SMEs), which generate more innovative ideas. Landström (2007) argues that venture capital funds are an important link in promoting the growth of innovative firms.

Venture capital funds mainly invest in small and medium-sized enterprises. With this support, they can develop their activities. Furthermore, they include financing at different stages of the undertaking's development, such as (Rosa, 2008):

- **Seed stage:** venture capital funds are reluctant to finance projects at this stage of development mainly due to the high level of the project's uncertainty.
- **Startup stage:** venture capital funds are keen to invest in startups, their product development, and initial marketing plans. At this development stage, firms often experience difficulties in obtaining a bank loan because of its faint credit background.
- **Early stage:** firms at this stage lack funds to enhance their position on the market and for further expansion. Venture capital especially funds enterprises at this stage of development, mainly due to the fact that a well-targeted investment offers great opportunities of significantly increasing the value of an enterprise in a short period of time.
- **Late stage:** at this stage, firms' value has already increased, and they require financial resources for larger investments. Nonetheless, these companies have rather limited access to venture capital.

Most scholars consider early-stage to be the classic form of venture capital. These funds invest in young enterprises by introducing a professional system of managing a given venture that covers all management cycles; including the most basic ones. At the seed stage, the role of VC is limited to supporting the development of a business idea before a product is introduced to the market; while, at the startup stage, the role of VC funds is limited to helping the consolidation of the project's market position. Early-stage projects highly depend on external resource providers due to the limited nature of their internal resource bases (Lockett et al., 2008).

The investor's decision to exit an investment often stems from a number of factors. Azarmi (2016) listed the fourteen most influential factors in venture capital's exit decision and ordered them into four main categories: (i) factors regarding investees, (ii) factors regarding venture capitals, (iii) factors regarding entrepreneurs, and (iv) factors regarding the external environment (see Table 1).

Table 1. The final list of the 14 most influential factors in a venture capital's exit decision

Category	List
Factors regarding investees	<ul style="list-style-type: none"> ▪ the NPV (Net Present Value) of the investee and its deviation from the venture capital's previous projections and current expectation, ▪ the investee's life cycle stage and if it passed its fast-growth stage, ▪ the comparison of the investee's performance with its updated business plan, ▪ the comparison of the investee's performance with the venture capital's quantitative and qualitative performance criteria, ▪ the assessment of the investee's financial status and its Altman Z-Score.
Factors regarding venture capitals	<ul style="list-style-type: none"> ▪ the attractiveness of the venture capital's alternative investment opportunities in comparison with keeping the current investment, ▪ venture capital's access to financial resources and its cache requirements, ▪ venture capital's contractual control rights and the existence of a put agreement, ▪ the availability of buyers interested in the investee.
Factors regarding entrepreneurs	<ul style="list-style-type: none"> ▪ the buyback ability of the entrepreneurs and the existence of a call agreement, ▪ the entrepreneurs' potential of attracting more funds and their previous records.
Factors regarding external environment	<ul style="list-style-type: none"> ▪ the priorities and preferences of the venture capital's fund providers and the capital markets, ▪ the financial legal system, ▪ the changes in the market of the investee's products/services.

Source: adopted from Azarmi (2016, p. 263).

Prior Studies Linking Venture Capital and Internationalization

Various empirical studies show that small and new enterprises may face problems with internationalization mainly due to the lack of both human and financial capital resources (Bilkey and Tesar, 1977; Bonaccorsi, 1992; McDougall and Oviatt, 1996; Oviatt and McDougall, 1994; Westhead et al., 2001). Unfortunately, there only is a handful of studies available that concentrate on the internationalization of venture capital backed companies. One of the first studies is by George, Wiklund and Zahra (2005), who analyze the importance of venture capital from a variety of perspectives. They

find that equity ownership can influence management's attitude toward the risk of internationalization. To examine this relationship, George, Wiklund and Zahra considered the impact of internal and external equity ownership on the scale and range of internationalization. They discovered that external equity ownership relates positively to the range and scale of internationalization measured by the number of countries, in which a firm establishes export relations, and the percentage of companies doing global business (George et al., 2005).

In turn, Zahra, Neubaum, and Naldi (2007) examine the impact of the presence of venture capital in the firm's ownership structure on internationalization. With the increase of the share of venture capital in the ownership structure of the enterprise – measured by the share of venture capital in the total capital – the activity for building knowledge and improving technological assets increases. Therefore, the presence of export-oriented venture capital can increase the activity of enterprises in the context of generating and acquiring international knowledge.

Another study on the internationalization of venture capital backed firms was carried out by a team of researchers from the University of Nottingham (UK). Lockett et al. (2008) analyze the export intensity of these companies, depending on their development stage: early stage (including seed and startup stage) and late-stage. They propose several hypotheses regarding the export activity of venture capital backed firms. In general, the researchers claim that the export intensity is the result of a strategic decision influenced by both the intellectual and financial capital of the firm. Lockett et al. also point to the role of management as one of the sources that can influence the intensity of export and allocation of resources in the venture. Venture capital funds with internationalization experience may be able to help the firm's management, in which they have invested, to select an appropriate strategy for entering foreign markets that, in turn, will contribute to the growth of its exports (Lockett et al., 2008).

Others consider the impact of the knowledge of venture capital funds on the startups' internationalization (Fernhaber, McDougall-Covin, 2009). They highlight the importance of international knowledge that can reduce the cost of internationalization that benefits startups in worldwide operations.

Furthermore, Hall and Tu (2003) foreground the willingness of venture capital firms to invest abroad as positively related to the size of the venture capital firm and the investment stage of their investees, as well as negatively related to the age of the venture capital firm. Other research shows that internationalization is not related to the type of venture capital firm ownership (Wright et al., 2005). Moreover, venture capital firms that operate

in a country with an active stock market are disposed to invest more internationally (Schertler and Tykvov'a, 2011; Aizenman and Kendall, 2012).

Based on the overview of prior studies in various parts of the globe, the author proposes to verify the following research hypotheses:

- H1:** Turnover of venture capital backed firms has a moderate influence on export value.
- H2:** Costs of employees play an important role in and positively correlate with export value explanation.
- H3:** Venture capital backed firm's export value is strongly positively linked with the number of employees in the analyzed firms.
- H4:** The share of shareholder's funds in operating income plays an important role in export explanation and strongly positively correlates with export value.

To verify, the author applied the hypotheses descriptive statistics, correlation and linear regression analyses with calculations in STATA 14.1.

Research Methodology: Data and Method

The data was obtained from Orbis-Bureau van Dijk. The database contains information about companies around the world and focuses on information about private companies, as well as presents companies in comparable formats. It holds information on around 250 million companies from all countries. Orbis collects information from more than 160 different providers and its added value is that all information are properly standardized and unified.

Table 2. Descriptive statistics

Variable	Description	Obs	Mean	Std. Dev.	Min	Max
exprev	Export revenue (in th EUR, 2016)	190	5 119.80	7 847.50	2	45 229
oprev	Operating revenue (in th EUR, 2016)	190	13 991.60	12 631.50	101	49 885
cemply	Costs of employees (in th EUR, 2016)	190	3 954.90	3 873.30	26	18 188
nemply	Number of employees (2016)	190	3.50	1.20	1	248
shfunds	Share of shareholders' funds in firms' income (2016)	190	1.83	7.59	0.02	81.50

Source: own calculations in STATA 14.1 based on data retrieved from Orbis.

The sample consisted of enterprises from the SME sector. Initially, the author selected 681 companies, financed by both private equity and venture capital funds that realized foreign sales. Subsequently, companies with incomplete data were eliminated. Out of the original sample size, eventually only 190 enterprises (Table 2) remained, mainly from France (64.2%), United Kingdom (27.4%), and other EU countries (8.4%), such as Estonia, Ireland, Germany, and Slovenia. These countries were selected mainly due to data availability: these enterprises had complete statistical variables that could be incorporated into the model.

In the next step, the author constructed four regression models, adopting as a dependent variable the value of export while, as independent variables, the operating revenue, costs of employees, the number of employees, and the share of shareholders' funds in total companies' income.

Empirical Findings and Discussion

The correlation analysis (Table 3) on the sample of 190 firms shows that there is a moderate positive dependence between the total turnover (oprev) and number of employees (nemply) of venture capital-backed firms, which means that the higher the turnover, the more willingly venture capital-backed firms hire new employees ($r = 0.6170$, $p < 0.001$), thus the costs of employees ($r = 0.6190$, $p < 0.001$) increase. Moreover, we see that there is also a moderate positive relation between the operating revenue (oprev) and export value. It turns out that the export value increases once a firm's turnover rises ($r = 0.6327$, $p < 0.001$). Finally, there is only a weak positive relation between the export value of venture capital-backed firms and their number of employees ($r = 0.3500$, $p < 0.001$).

Based on the correlation matrix (Table 3), we notice that there is a strong positive relationship between the costs of employees of venture capital backed firms and their turnover ($r = 0.6327$, $p < 0.001$) rather than export value ($r = 0.5382$, $p < 0.001$). Noteworthy, the share of shareholders' funds in total firms' income correlates *negatively* with firms' export value ($r = -0.0657$, $p < 0.001$) and their number of employees ($r = -0.2224$, $p < 0.001$).

The data in Table 3 show that there is no multi-collinearity between defined independent variables. For more accuracy, the author also checked whether the variance of the given independent variables is correctly explained by the variance of other independent variables (Table 4). In our case, the tolerance value is between 0.5166 and

0.9478, which means that the established model is good. Ćuzović et al. (2017) claim that – when value of this indicator is lower than 0.1 – it indicates the existence of multi-collinearity.

Table 3. Correlation matrix

	Exprev	oprev	cemply	nemply	shfunds
Exprev	1.0000				
Oprev	0.6327*** (0.0000)	1.0000			
Cemply	0.5382*** (0.0000)	0.6190*** (0.0000)	1.0000		
Nemply	0.3500*** (0.0000)	0.6170*** (0.0000)	0.5810*** (0.0000)	1.0000	
Shfunds	-0.0657 (0.3678)	-0.1081 (0.1376)	-0.0894 (0.2198)	-0.2224** (0.002)	1.0000

p-value in parentheses.

* p < 0.05, ** p < 0.01, *** p < 0.001.

Source: own calculations in STATA 14.1 based on data retrieved from Orbis (n = 190).

Table 4. Multi-collinearity test (VIF)

Variable	VIF	Tolerance (1/VIF)
oprev	1.94	0.5166
cemply	1.88	0.5327
nemply	1.81	0.5521
shfunds	1.06	0.9478
Mean VIF	1.67	

Source: own calculations in STATA 14.1 based on data retrieved from Orbis (n = 190).

For the purpose of this article, four linear regression models were created in STATA 14.1, by considering one, two, three or four independent variables accordingly. The author used export revenue as a dependent variable.

According to the first regression model (Table 5), the higher the turnover (oprev) of venture capital backed firm, the higher its export value. The rise in operating revenue

by one unit results in the average exports increase of 393 EUR (statistically significant at the level of 0.001), assuming that the other independent variables remain unchanged.

Table 5. Linear regression models

Dependent: <i>exrev</i>	(1)	(2)	(3)	(4)
<i>oprev</i>	0.393*** (-0.0614)	0.302*** (-0.0809)	0.343*** (-0.0853)	0.343*** (-0.0855)
<i>cemply</i>		0.482* (-0.235)	0.585* (-0.246)	0.586* (-0.247)
Natural logarithm <i>nemply</i>			-1010.2* (-458.7)	-1037.9* (-473.0)
<i>shfunds</i>				-2.903 (-1.845)
_ cons	-379.6 (-545.9)	-1005.2 (-542.4)	1577.2 (-1004.3)	1679.4 (-1065.4)
N	190	190	190	190
R-sq	0.400	0.435	0.449	0.449
adj. R-sq	0.397	0.429	0.440	0.437
F	40.94	25.81	18.62	24.84

Robust standard errors in parentheses.

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$.

Legend:

exrev – export revenue (in th, 2016)

oprev – operating revenue (in th, 2016)

cemply – costs of employees (in th, 2016)

nemply – number of employees (in 2016)

shfunds – Share of shareholders' funds in total firms' income (2016)

Source: own calculations in STATA 14.1 based on data retrieved from Orbis (n = 190).

In the second regression model, the author selected two independent variables: turnover and costs of employees in venture capital backed firms. Like in the first model, turnover positively influences export. Moreover, when the costs of employees rise by one unit (which means 1000 EUR), the export value of venture capital backed firm increases by 482 EUR (significance at the level of 0.05).

In the third regression model, what is puzzling is that natural logarithms of the number of employees (significance at the level of 0.05) can contribute to a reduction in export. There can be many reasons for this situation. One of them has been presented by

Leichenko (2000) who claims that export growth contributes to employment reduction. Leichenko questions whether this employment reduction is associated with export-related increases in labor productivity. Research over the last few years confirmed Leichenko's suspicion: productivity can help explain the negative correlation between export growth and employment. A few years later empirical analysis of Kilkenny and Partridge (2009) shows that there is a negative relationship between the export sector employment and its growth. It seems to confirm the thesis that venture capital backed firms engage in increasing labor productivity.

In comparison to the third regression model (Table 5), the fourth model applies an additional variable: the income of the share of shareholders' funds in venture capital backed firm (shfunds). The model shows the impact of this variable on export value. When the share of shareholders' funds in total income rise by 1000 EUR, the export value decreases by almost 3000 EUR, but the variable is not statistically significant.

Conclusions

Venture capital funds are the main source of funding for innovative ventures. In Europe, the market for these funds is different from the one appearing in the United States of America. In Europe, venture capital finances companies at early stages of development, while in the USA they finance companies that already have great experience (late stage of development).

Statistical calculations confirm two out of four hypotheses (Table 6). The research shows that the turnover of venture capital backed firms positively influences their export value. Moreover, both costs of employees also play an important role in the export value explanation. Nevertheless, the empirical study did not confirm that export value of analyzed firms strongly positively correlates with the number of employees and their share of shareholders' funds in operating income.

Few researchers considered the subject of export of venture capital backed firms. One of the most famous articles about the export intensity of venture capital backed firms, by Lockett et al. (2008), argues that export intensity results from a strategic decision, influenced by both the intellectual and financial capital of the firm. Whereas Devigne, Vanacker, Manigart, and Paeleman (2013) examine whether the presence of cross-border versus domestic venture capital investors is associated with the growth of portfolio companies.

Table 6. Hypotheses verification

Hypotheses	Verification	Methods
H1: Turnover of venture capital backed firms has a moderate influence on export value.	confirmed	Regression analysis Correlation analysis
H2: Costs of employees play an important role in and positively correlate with export value explanation.	confirmed	Regression analysis Correlation analysis
H3: Venture capital backed firm's export value is strongly positively linked with the number of employees in the analyzed firms.	not confirmed	Regression analysis Correlation analysis
H4: The share of shareholder's funds in operating income plays an important role in export explanation and strongly positively correlates with export value	not confirmed	Regression analysis Correlation analysis

Source: own elaboration.

The research has a number of implications for practitioners. The above study shows that the increase in the value of exports is accompanied by an increase in the costs of employees. With the decision to expand to new markets, the company bears the increased costs resulting from “being new on the market.” These costs may be related, among others, to hiring experienced staff and increasing the expenditure on basic salaries (Zaheer, 1995; Gomez-Mejia and Palich, 1997; Ruigrok and Wagner, 2003).

Research limitations

The analyzed period was limited only to 2016. Second, the study used only one dependent and four independent variables. Further research must include other variables, especially moderating ones, such as entrepreneurship ratio or availability of external financing forms. Third, the regression models were based on data retrieved from Orbis Database and can induce uncertainty regarding its credibility.

Direction for further studies

At present, there are still only few research studies that explore the export of venture capital backed firms. Therefore, the next steps should be to focus on exporting motives of those firms in order to better understand the phenomenon of VC backed companies. However, the author highly recommends using more independent variables in further modeling.

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