

SSE Riga
Thesis Presentation

● “SMART” vs “DUMB” MONEY:

Perceptions about Venture Capital of
Latvian Start-Ups and High-Growth Firms

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EXECUTIVE SUMMARY

- Research focus: entrepreneurs' perceptions of VC value-added
- Market stakeholder interviews & a demand-side survey
- Approached **1202** high-tech / high growth firms
- **5.16%** complete response* rate (***62** complete responses)

Discovered MOTIVES in the VC financing decision:

AGAINST

- Perception that local VCs lack technology competence
- Individual reasons for starting the venture
- Past experience

FOR

- “Dumb money” (only money)
- Networking opportunities (especially abroad)

INITIAL OBSERVATIONS OF THE LATVIAN VC MARKET

- Early stage of development
- Several public funds
- Many firms in demand, but funds report low dealflow
- Stakeholders unable to pinpoint causes of market mismatch / gaps / asymmetries

● RESEARCH & KNOWLEDGE GAP

○ Value from this research added to:

- **Industry efficiency**: decrease asymmetries between supply & demand
- **Economic rationale**: the Latvian taxpayer
- **Academic community**: local AND global lack of research on demand for VC

INTERVIEWS

SUPPLY

Latvian VCs

- FlyCap
- Eko Investors
- Imprimatur Capital

LGA - public VC oversight body

LVCA

DEMAND

infogr.am

ask.fm

FROONT

MaxTraffic

tech hub

RESEARCH TIMELINE



INTERVIEW &
SURVEY
DESIGN

2014 Aug



INTERVIEWS
WITH SUPPLY
& DEMAND
AGENTS

Nov-Mar



FINALIZING
THE SURVEY

2015 Feb



SURVEY SENT
TO **1202**
ventures

2015 Mar



VENTURE CAPITAL

SMART MONEY: more important than how much money you get is whom you get it from.

● VENTURE CAPITAL

- Capital for high-risk seed, startup, early or growth ventures
- In developed VC markets usually hi-tech and/or high growth:

Life Sciences



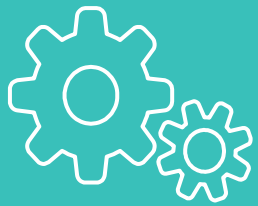
ITC



● TECH STARTUPS

TBNVs:

Technology-based new ventures



Tech investors:

Funds who have an applied tech background (industry experience) and who invest in the technology rather than the team

● TECHNOLOGY INVESTORS: SMART MONEY



Have experience in the respective industry (nanotechnology, software)



Better understand the product/service leading to more accurate valuations



Provide business networks (clients & further financing)

Bottom line: technology investors invest in the **idea** rather than the team

● SMART MONEY

= Non-financial value-added

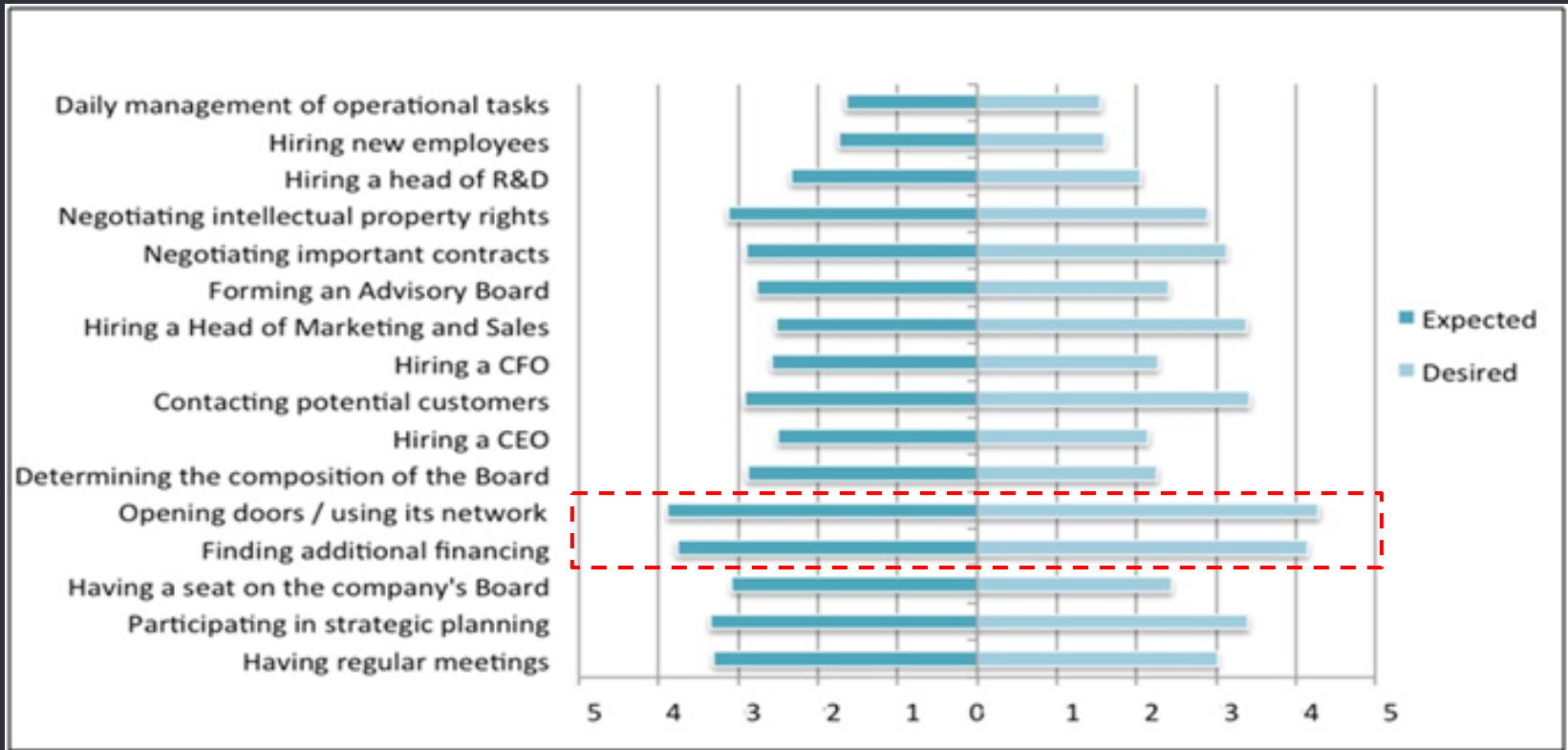
Decomposition of types of value-added activities:

- Consulting / konsultēšana
- Mentoring / mentorings
- Strategizing / stratēģijas izstrāde
- Mandating / norādījumu sniegšana
- Operating / uzņēmuma darbības jautājumi
- Recruiting / darbinieku atlase

Source: (Mason & Kwok, 2010)



DEMAND SIDE: PERCEPTIONS vs EXPECTATIONS



Source: Authors' research

● DEMAND SIDE: PERCEPTIONS vs EXPECTATIONS

○ PROVIDED

- Financial know-how
- General Management Experience
- Monitoring

IN DEMAND

- Business Networks
- Technology Know-How

● Demand side: Perceptions of Latvian VCs

○ Latvian VCs lack 'classic' VC skills:

- do not add sufficient non-financial value
- screening effectiveness can be improved
- high fund manager turnover rate
- VCs lack ITC, life-sciences and engineering backgrounds

○ Monitoring activities are insufficient:

- high fund manager (fund employee) turnover rate → lack of continuity
- VCs sit on boards, but rarely engage in 'value-added' activities

● Supply side: Perceived problems

- Low dealflow
- Lack of investment-ready projects
- Entrepreneurs are averse to losing control and/or cash-flow rights
- Entrepreneurs mistrustful of VCs, their motivations and intentions
- VCs are involved in raising companies' investment-readiness & educating firms

○ Comment:

- Lack of focus among past public venture capital investments

“

“Foreign investors have different valuation practices; the valuations we receive from local investors are considerably lower compared to those of foreign investors.”

--Founder of several startups



RESULTS:

Reasons for seeking cross-border financing

Motives to attract foreign
venture capitalists

Experience in high tech
industries

◦ Strong in-house technology
investor teams

Established track record
& business network

◦ Higher valuations & greater
post-financing stage
involvement

Client attraction &
access to further
financing

RESULTS: AVERSION TO LOSING CASH FLOW AND CONTROL RIGHTS

REASONS FOR FOUNDING A COMPANY

Independence

Making money

Financial security

VENTURE FOUNDERS' MISTRUST OF VCS

Lack of investment readiness

LACK OF TECHNOLOGY INVESTORS

Latvian VCs unlikely to alter the founding management team

RESULTS: PUBLIC VENTURE CAPITAL FUNDS

- Crucial for developing the ecosystem and providing financing at the pre-seed and early stage ventures
- Policy documents should specify target industries (e.g. high tech and life sciences)
- .. or an investor base with experience in the respective industries.

“

“If you want to get the venture capital market going, you need long term government involvement in public VC funds to get the market going.”

--David Sonnek, Head of SEB Venture Capital

“

“You also have to create buzz.

People, investors included, are not as much driven by rationality as by compelling stories.

You have to establish Riga as an alternative to Israel that capitalizes on their engineers, where the smartest people and excellent infrastructure can be found.”

--David Sonnek, Head of SEB Venture Capital

● CONCLUSIONS

To eliminate asymmetries

- **Latvian VCs** can add value by **providing networks & attracting additional financing**
- Obtaining tech skills - long & difficult process

To improve the ecosystem

- **Policy makers** can help **spread the Latvian startup success story**
- **Attracting cross-border VC** - more cost-efficient for small countries than developing locally?
- VC funds working with **public money** should focus on **startups** with potential for **high growth & international aspirations**

To receive financing & value-added

- **Entrepreneurs** MUST increase **investment readiness**

Thank you!

QUESTIONS ARE WELCOME!