The Impact of an Entrepreneurs' Social Capital on Government-Sponsored Venture Capital Decisions

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Managing a public sector is difficult. Bureaucratic inefficiencies and political and social pressures are aspects that resulted in the need for the governments' intervention initiatives (Lermer 2009). Although government-sponsored venture capital funds usually are not short of money, a higher number of successful entrepreneurs get funded either through private or not-for-profit venture capitalists. In order to better understand the issues of government venture capital and provide recommendations for public policy and execution, this research is dedicated to exploring and assessing the performance of government-sponsored venture capital firms and comparing them to the private and not-for-profit venture capitalists. This will be done through the lens of social capital and the resource-based view.

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Venture capital is a "professionally managed pool of money raised for the sole purpose of making actively-managed direct equity investments in rapidly-growing private companies" (Megginson 2004, p. 89). If the private company is successful, the venture capital firm has the potential to earn a profit through the equity invested. However, it is not just the money that entrepreneurs get from venture capitalist's (VC's) in exchange for equity share. VC's also offer a wealth of expertise through not only themselves, but their professional network, which is very important to entrepreneurs (Bottazzi, Da Rin, and Hellmann 2004; Gompers 1995; Hellmann, Thomas, and Puri 2002; Lindsey 2003).

Venture capital is an important factor that fueled the economic growth of entrepreneurial platforms in areas such as Silicon Valley in the United State and Singapore in Asia (Bottazzi, and Rin 2002; Samila, and Sorenson 2011). Alternatively, slow economic growth in places such as Florida and Alaska in the United States, and in other parts of the world has been attributed partially to the lack of venture capital that is available (Samila, and Sorenson 2011). According to the National Venture Capital Association (2009), the income from venture capital backed enterprises is responsible for 21 percent of the United States Gross Domestic Profit (GDP), as well as providing 11 percent of private sector jobs.

Even though the majority believe that private sector and freedom of market have led to thriving entrepreneurial activity (Friedman 1970), especially in places such as Silicon Valley (Prusa, and Schmitz 1994), public effort and intervention have played a crucial role in stimulating the entrepreneurial development (Lerner 2009). For example, Silicon Valley and Dubai, among others in the world, are recognized as entrepreneurial hubs where private investors

and entrepreneurs can meet to develop opportunities into success. This does not necessarily mean that the Government did not play a significant role as well.

The role of Government-sponsored venture capital in Silicon Valley, Dubai

There are many factors that have led to the success of Silicon Valley. One of the main and crucial factors is government intervention, particularly in stimulating the venture capital industry (Lerner 2009). Tracing back to the time of the Great Depression (1930), when businesses and government officials realized that existing forms of financing were unsuitable and there was a need of a new way of financing other than banks and the independently wealthy (Gorman, and Sahlman 1989), the idea of venture capitalists emerged.

The first formal venture capital firm, "American Research and Development" (ARD), was formed in order to provide a new form of financial assistance. Ralph Flanders, who at the time was the head of Federal Reserve of Boston, publicized the need for and recruited business leaders to build new enterprises to help finance newly established businesses in 1946 (Lerner 2009). The next venture capital experiment was the Small Business Investment Companies (SBICs), which was federally guaranteed risk capital pools of money in the 1960s (Lerner 2009). These initiatives paved the way in the development of many venture-minded firms in Silicon Valley in an effort to help jump start well-known businesses of today, such as Venture Economics, Apple Computer, Compaq (Hewlett-Packard), and Intel.

Dubai is another example that has benefited from public intervention. According to the Dubai Statistics Center (DSC), SMEs (small and medium-sized enterprises) account for about 95 percent of the total enterprise population in Dubai and they employ around 42 percent of Dubai's workforce (Gutcher 2014). They also contribute about 40 percent of the state's income (Gutcher

2014).

The governments' role in advancing the economy is much more clearly understood in Dubai. It started in the 1950's when Sheikh Rashid bin Saeed Al Maktoum, the governor of Dubai at the time, envisioned Dubai as one day being the main trading hub in the region. He ensured the development of their port by dredging Dubai's creek in order to enhance Dubai's trading and exporting position with a loan from Kuwait. Trading and exporting increased so rapidly after the project completion and Dubai was able to repay the loan soon after (Lerner 2009). This successful step was followed by another ambitious move to establish the Jebel Ali port to allow for much larger ships, such as global shipping vessels (Lerner 2009). Moreover, the Dubai's Internet City (DIC) was established in the early 2000's as a way to bring many new businesses to live there, through their incentive programs. These incentives were very enticing, as one of the main things was the ability to earn tax-free profits for at least 50 years. These moves, coupled with others government interventions, especially in the government venture capital, helped create an entrepreneurial-friendly environment that resulted in Dubai being viewed as an entrepreneurial hub (Lerner 2009).

Silicon Valley in the United States of America (USA) and Dubai in the United Arab Emirates (UAE) used government interventions and venture capital so wisely to boost economic growth, innovation, and job creation, that governments around the world tried to replicate and stimulate the venture capital industry in order to get similar results in their own areas (Megginson 2004). Singapore, for example, adopted policies toward entrepreneurship and created public venture capital in order to increase economic growth (Lerner 2009). Other examples where this was replicated include Silicon Valley of India Bangalore (Dossani, and Kenney 2002) and parts of Brazil (Ribeiro, and Carvalho 2008).

Focus of Study

Managing a public sector is difficult. Bureaucratic inefficiencies and political and social pressures are aspects that resulted in the need for the governments' intervention initiatives (Lermer 2009). Although government-sponsored venture capital funds usually are not short of money, a higher number of successful entrepreneurs get funded either through private or not-for-profit venture capitalists. For example, Bab Rizq Jameel's initiative is a not-for-profit venture capital firm that has operated in Saudi Arabia since 2003. Since its inception, it funded more than 25,000 entrepreneurs to start a business and helps to provide more than 345,000 jobs, where about half of them were for women (Hesah Al-Shaikh 2013). These numbers surpass the rest of the entrepreneurs of all Saudi Arabia public venture capital funds combined. This is also true for government-sponsored venture capital firms in the United States and different parts of the world.

In order to better understand the issues of venture capital and provide recommendations for public policy and execution, this research is dedicated to exploring and assessing the performance of government-sponsored venture capital firms and comparing them to the private and not-for-profit venture capitalists. This will be done through the lens of social capital and the resource-based view.

Social capital theory suggests that access to a network and social ties are considered valuable resources to the entrepreneur (Singh, Hills, Lumpkin, and Hybels 1999; Zane 2011). Social capital is defined as the "sum of actual and potential resources embedded within, available through, and derived from the network of relationships possessed by individuals or social units." (Nahapiet, and Ghoshal 1998, p. 243).

The resource-based view suggests that access to human capital, knowledge, and financial capital provides entrepreneurs with a path to success (Alvarez, and Busenitz 2001; Zane 2011).

Entrepreneurs recognize opportunities through their different perspectives of the value of available resources (Schumpeter 1934; Kirzner 1979; Shane, and Venkataraman 2000, Alvarez, and Busenitz 2001*)*.

Entrepreneurs may use their social networks to gain access to resources and funding. Entrepreneurs have different options to gain funding, which include private venture capital, not-for-profit venture capital, banks, and public or government venture capital. Since literature suggests that entrepreneurs benefit from social networks to access financial resources (Batjargal, and Liu 2004; Gopalakrishnan, Scillitoe, and Santoro 2008), the focus of this research is to answer the question: what is the relationship between entrepreneur's initial social network and the access to public venture capital funds? Also, the research focuses on the unique resources that entrepreneurs receive from government-sponsored venture capital, as suppose to the private one.

Very few studies have looked into how resources, especially the source the financial resource, influence performance (see Eddleston, Kellermanns, and Sarathy 2008; Sirmon, Gove, and Hitt 2008; Sirmon, Hitt, and Ireland 2007; Kellermanns *et.al.* 2014). Financial capital, also known as financial resources, has been discussed in concurrence with other resources that include human, financial, physical, and relationship capital (see Brinckmann and Hoegl 2011; Clarysse, Bruneel, and Wright 2011). Little attention has been paid solely to venture capital, particularly the government-sponsored venture capital, as a source of financial capital and its relationship to performance.

The contribution of this research is to enhance the understanding of the role of government-sponsored venture capital in an effort to build friendly ecosystem's that try to promote more entrepreneurs to start a new business from the perspective of social capital and

resource-based view. This research will investigate the differences between government-sponsored and private venture capital, and how different sources of venture capital have varying impacts on the performance. In addition, the research will evaluate the performance of the Silicon Valley's government-sponsored venture capital in the USA, UAE, and Saudi Arabia. Lastly, the research will provide recommendations and guidelines for the leaders of the government-sponsored venture capital funds as ways to improve their efficiency and productivity.

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