Venture Capital
Run by Private or Governmental Interests

A Comparative Study on the Investment Decision Process in the Swedish Market

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Patrick Schwaiger (40688) and Amanda Tunberg (22265)
Supervisor: Mikael Samuelsson
Examiner: Karin Fernler

Abstract

Governmental and private venture capital firms have been known to differ in various ways. There is research on the differences in goals, performance and post-investment behaviour of those two kinds of organisations but none examining and comparing their investment decision process. This thesis builds on previous research in the field and explores the question of how the differences in the motivation of employees and investment goals between governmental and private venture capital funds in Sweden influence the investment decision process. An in-depth qualitative study consisting of interviews with the major governmental and private venture capital firms in Sweden as well as a number of entrepreneurs was deployed. In line with previous publications, the results show that private VCs have only financial goals while the governmental VCs pursue more strategic goals like the creation of employment or the stimulation of the economy. Furthermore, in order to reach their respective goals, different incentives to increase the employees' extrinsic motivation are applied. Private VCs try to motivate their employees with monetary incentives like bonuses or the participation on the upside of an investment. Governmental VCs on the other hand have less focus on monetary incentives. Furthermore, the study provides the insight that the differences in goals and employee motivation mainly affect the deal origination and screening stage of the investment decision process. Due to their goal of educating the market, governmental VCs spend a lot of time for screening every incoming application for funding. This extensive process reduces time to actively search for potential investments. In the private sector the monetary incentives encourages the employees to actively search for promising investment opportunities.

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Core Concepts

Closed-end funds: Funds with a limited, predetermined time horizon for their investments.

Evergreen fund: A fund that is supposed to reinvest all the earnings and survive indefinitely without any additional capital injections.

Fear of missing out (FOMO): When a person or group of people participate in an activity or process because non-participation produces the anxiety that one might misses something funny or important.

Governmental Venture Capital Company (GVC): A VC that gets its funding from the government. GVCs are founded by the government but not necessarily run by the government.

Open-end funds: Funds with an unlimited time horizon for their investments.

Private Venture Capital Company (PVC): A privately owned VC company. PVCs are owned either by a corporation, a bank or individuals. Additionally, they raise their funds from private sources.

Start-up: A newly started company, generally thought of as innovative.

Venture Capital (VC): Independently managed, dedicated pools of capital that focus on equity or equity-linked investments in privately held, high-growth companies (Lerner, 2009, p. 6-7).

1 Introduction

New ventures are seen to be particularly innovative and innovation is critical for economic growth. Researchers have found a strong connection between technological progress and economic prosperity (Lerner, 2009, p. 44-45). For the reason that economic growth is stimulated with new companies, it is of special interest for policy makers to promote the foundation of start-ups in a country. That is why the governments here in Sweden, and in many other countries all over the world, try to find good avenues to stimulate small companies. They offer training, cheap loans, incubation, acceleration and venture capital (VC) investments, all financed by tax money. The foundation of governmental venture capital firms can be viewed as a failure of the private sector to adequately supply funding to the market (Brander, Egan, & Hellman, 2008). In addition, when it comes to the support of new ventures, the public sector is considered to be important to stimulate entrepreneurial activity. However, on a global scale more often than not, governmental interventions have been failures (Lerner, 2009, p. 7).

Given the facts that many govenmental venture capital programs fail and that there are a number of successful private players in the VC industry in Sweden a skeptic might raise the questions if tax money should be used for venture capital investments and if a governmental fund has the legitimacy to exist. Put in a different way this means that if the government is not trying to build something big, that could potentially earn a huge amount in taxes and employ a great number of people, then why use the money this way. In that case the taxes might as well be redistributed in a different way for example to improve child support and education or to increase pensions.

1.1 Industry Background

Stockholm is the "second most prolific tech hub in the world behind Silicon Valley" (Davidson, 2015). Home to what is known as the five unicorns[1] Skype, Mojang, Spotify, King and Klarna, Stockholm has emerged as one of the hotspots for tech innovation. In line with the thriving start-up scene, the Swedish venture capital industry has become one of the top 10 most active in the world measured as investments against GDP (Lerner & Tåg, 2013). During 2015, a total of 1,1 billion dollars in equity investments have been raised by private Swedish tech start-ups, making Sweden the number one amongst its European peers when looking at the invested capital and deals per capita (figure 1). Although this numbers are highly affected by Spotify's 526 million dollars series G financing deal, they still show the popularity and success of Swedish tech entrepreneurs. Considering the origin of the capital, angel investors and venture capital companies (public as well as private) are by far the most important source of funding in Sweden, accounting for 45% and 40% of the total invested capital respectively (Industrifonden, 2016).

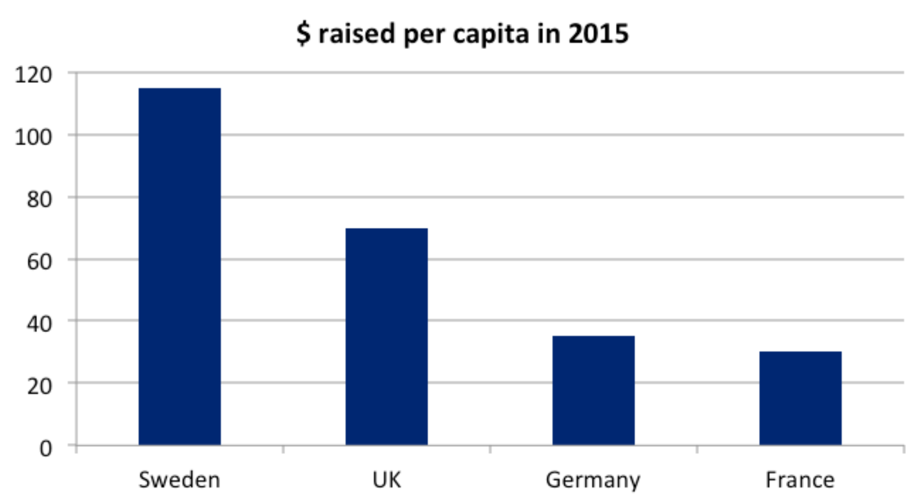

Figure 1: Money raised per capita in European countries (Industrifonden, 2016)

[1] A unicorn is a company that has reached a valuation of $ 1 billion or more.

New innovative ideas are popping up everywhere, fighting for the investors' attention. Newly funded ventures searching for seed financing had a number of investors to choose from while later stage companies experienced more difficulties raising a new round in 2015 (Industrifonden, 2016). This shows that investors are seeking to take very high risks in search for potentially high returns. Given the thriving start-up industry here in Sweden, the venture capital environment is considered an interesting field to do research in.

1.2 Research Topic, Purpose and Question

The purpose of this thesis is to shed light on the best way to organise a governmental intervention program such as a governmental venture capital firm. Therefore, the Swedish VC market is studied. The study focuses on the differences between the private and governmental VC firms and examines if the differences in goals between the two entities ultimately influence their investments. This is done by analysing the impact that the goals have on the employees', more specifically on their motivation to perform in their job, and how the investments decision process is adapted to implement the differing goals.

Several papers have sought to find the effect of governmental venture capital on the performance and future funding of a new venture as well as the difference of the effects to a private venture capital firm (Brander, Du & Hellmann, 2015; Lerner, 2009; Lerner, 1999; Lerner & Tåg, 2013). The evidence from research into the structure and behaviour of VC funds suggests that there are some differences in behaviour between governmental venture capital funds and private venture capital funds and that these are related to the differences in goals of the two (Luukkonen, Deschryvere & Bretoni, 2013; Brander, Du & Hellmann, 2015; Lerner, 2009). In addition to having different goals with their investments, the governmental venture capital funds have employees with a different level of motivation (Knockaert, Lockett, Clarysse, & Wright, 2006). The difference in goals has an impact on the motivation of the employees, as it is a form of extrinsic motivation. Building on an extensive amount of research concerning the comparison of private and public venture capital funds, this thesis aims at answering the following question:

How do the differences in the motivation of employees and investment goals between the governmental and private venture capital funds in Sweden influence the investment decision process?

From a venture capital firm's perspective this is interesting because goals are categorised as extrinsic motivators. Since both goals as well as extrinsic motivation of employees can be actively influenced, it is useful to know how they affect the investment decision process. If one is aware of the mechanisms behind the motivation of one's employees, one can align goals, motivation and the investment decision process and thereby maximize efficiency and performance. For policy makers this is of special importance to make informed decisions about the governmental venture capital funds setup and structure as well as to assess if the tax money is used in an efficient way when invested in a governmental venture capital fund. To properly design successful public funds is in the taxpayers' interest, which is also why this research is so important. From an entrepreneur's viewpoint taking a look at the issue at hand is of interest, the differences in employee motivation and goals of a venture capital firm, gives information about how the different VCs behave during the evaluation and negotiation process.

In order to answer the research question and fill the prevalent research gap the remainder of the paper is structured in the following way: in the second section, the relevant theory is reviewed to provide an overview of the previous research done on the venture capital and start-up industry as well as on motivational concepts. It concludes with the identification of the research gap and the presentation of the theoretical framework for the research. Within the methodology section, the applied research approach is outlined. The subsequent part focuses on the presentation of the empirical data gathered from the conducted interviews. In section five the results of the research are analysed in the light of the relevant theory in order to answer the research question. The last section of this thesis is dedicated to the discussion and a general conclusion of the findings.

2 Literature Review

The literature review is structured in the following way.

Human Capital

In the thirst section (2.1) human capital is introduced. The focus lies on theories on employee motivation. A common basis is established by introducing the resource-based view, where the importance of human capital is highlighted. Furthermore, it is elaborated how differences in employee motivation influence the human capital. The connection between goals and human capital lies in motivation. It is essential to understand the nature of motivation and how it is affected by organisational goals. It is the human capital i.e. the employees that perform the decision making process and therefore, shape it.

Ways of funding

Section 2.2 provides a simple outline of all the available ways of funding a new venture. Furthermore, the different sources are characterized and explained according to the findings of previous research. This enables the reader to put venture capital funding in the bigger context of all possible funding sources.

Venture Capital

The third part of the literature review outlines the origin of venture capital and what different forms of venture capital exist (2.3). The purpose is to dig deeper into this specific way of funding and create an understanding of the differences between the various forms of venture capital. Furthermore, the investment decision process a VC firm undergoes until it decides to invest in a new venture is described. This section outlines the existing research done surrounding the research question.

The literature review ends with describing the identified research gap and introducing the theoretical framework applied to address this gap.

2.1 Human Capital and the Resource-Based View

When trying to understand organizational performance it is important to consider human capital (Dahlqvist, Davidsson & Wiklund, 2000; Gimeon, Folta, Cooper & Woo, 1997; Ucbasaran, Wright & Westhead, 2003). Human capital theory suggests that humans with higher levels of human capital preform and execute tasks better, and this includes executives in venture capital investments (Dimov & Shepherd, 2005). Zarutskie (2010) states, based on the resource-based view of the firm that human capital matters to investment performance. In organizations where the people are the most valuable resource human capital becomes very important (Zarutskie, 2010). The resource-based view suggests that the resources available to a firm are what provide the firm the competitive advantage necessary to outperform the competition (Penrose, 1959).

There are slightly different definitions on human capital, but commonly it is the idea that different skills, knowledge and education make (Knockaert, Lockett, Clarysse, & Wright, 2006) employees have different economic value (Becker, 1975). A company can increase the human capital by fostering the development of its employees or similarly a country as a whole can improve human capital by investing in its education system for instance. In the venture capital research several papers examine the importance of human capital in VC firms. Dimov and Shephard (2005) investigate the relationship between education and experience of VC firms' partners and find that some aspects of human capital contribute to some but not all dimensions of performance. Research suggests that certain parts of the human capital in different venture capital organisations were proven to have striking similarities. These parts include education level, past experience, and values (Zarutskie, 2010).

Besides the education and skill level of the employees, their motivation is also a major part of human capital. Unmotivated employees are more inclined to change their employer, tend to put less effort in their work and consequently fulfil their tasks with a lower quality. Highly motivated workers, on the contrary, are more likely to be persistent, creative and deliver qualitatively better results (Amabile, 1993). Hence, motivation is not only a part of human capital itself, but also a decisive factor influencing how the employees make use of their capabilities. Therefore, motivation is probably the most important part of human capital.

To further analyse the concept of motivation the Self-Determination Theory is consulted. This theory divides motivation into two principal types: intrinsic and extrinsic. Intrinsic motivation is the act of doing an activity for the inherent satisfaction, whereas extrinsic motivation is the act of doing an activity for some separable consequence of outcome (Deci & Richard, 1985). The following section characterises those two sorts of motivation and combines them with Maslow's Hierarchy of Needs and Herzberg's Two-Factor Theory.

2.1.1 Intrinsic and Extrinsic Motivation

One focus of previous motivational research takes more the psychological perspective on the difference between intrinsic and extrinsic factors of motivation into account. In this categorization, intrinsic motivation refers to an individual's value for the work itself (e.g. interest in the task) while extrinsic motivation is developed by the desire to obtain a specific output (e.g. rewards) that is detached from the work itself. Both affect the way employees do their work however, the effect on subjective feelings towards the work can be very different (Amabile, 1993).

2.1.1.1 Intrinsic Motivation

Intrinsic motivation was first discovered in studies of animal behaviour, when it was observed that animals sometimes engage in playful or curiosity-driven behaviours without any type of reinforcement or reward. In humans, this natural tendency to explore and learn is critical for cognitive, social and physical development. Intrinsic motivation is, therefore, often argued to be the most important form of motivation. Intrinsic motivation is an inherent disposition that cannot be artificially created. Therefore, research on this topic is mainly focused on how to catalyse intrinsic motivation. The goal of the Self-Determination Theory (SDT) is to provide a framework for social and environmental conditions that sustain or enhance intrinsic motivation, as well as determine under what conditions intrinsic motivation can be undermined (Deci & Ryan, 2000).

The Cognitive Evaluation Theory (CET), a subtheory of SDT, outlines a number of factors that can influence a person's intrinsic motivation. Events that induce feelings of competence, such as efficient and non-demeaning feedback, enhance intrinsic motivation since they satisfy a basic psychological need of self-efficiency (Deci & Ryan, 2000). Several studies support this theory by showing that positive feedback on performance has a positive effect on intrinsic motivation while negative feedback has a negative effect (Deci, 1971; Deci & Cascio, 1972). CET also argues that inducing feelings of competence is not enough to increase intrinsic motivation, unless accompanied by a sense of free will. CET proposes that intrinsic motivation can be facilitated or undermined by facilitating or undermining feelings of autonomy and perceived competence (Deci & Ryan, 2000).

Even though intrinsic motivation can be argued to be the most important type of motivation, it ultimately only exists when individuals inherently hold a value for a behaviour or an activity. This is important to take into consideration since many behaviours required or preferred by society, such as motivating children to learn or getting individuals to quit smoking, may not hold intrinsic value for all individuals. Therefore, in many cases, it becomes necessary to look at extrinsic motivators. Furthermore, Amabile (1993) states that even though "there may be some activities (for some people, in some jobs) that are purely intrinsically motivated, this case is almost certainly more rare", resulting in a high probability that for most work related tasks intrinsic as well as extrinsic motivators are present.

One of the most used models in the context of motivation is Maslow's Hierarchy of Needs (figure 2) (Maslow, 1943). The model describes humans' needs in a pyramid. It is a good depiction of an intrinsic motivation model. The first step consists of the most basic physiological needs – food, water and shelter – that all humans need to survive. On the second layer safety needs like protection against danger and threats are depicted. The third step consists of the social needs love and friendship. Ego needs, a need to achievement, adequacy and freedom show up on the fourth layer. One could describe this as the need for independence. In addition, status and recognition, the needs for self-esteem or self worth are included in this category. On top the hierarchy are the self-actualization needs, the need to realise ones own potential and become more of what one is capable of becoming (Pardee, 1990).

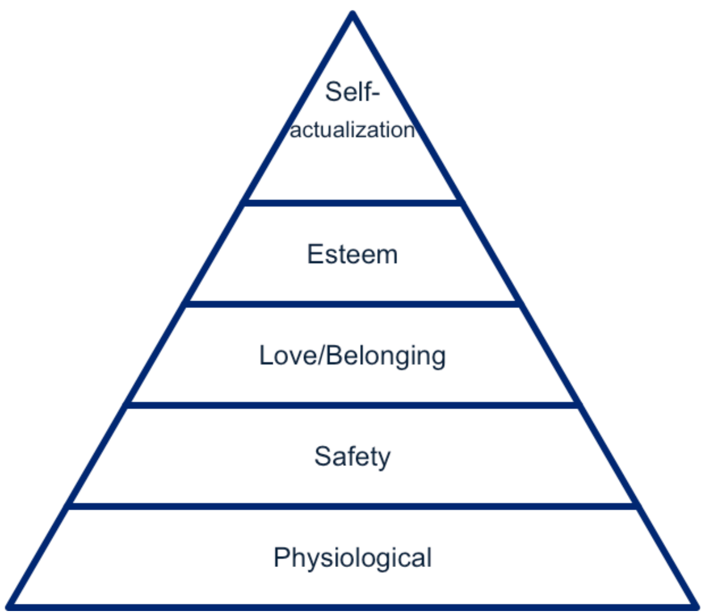

Figure 2: Maslow's Hierarchy of Needs (Maslow, 1943)

There are two conclusions that can be drawn from this model that are important in relation to motivation, these are: If the need is satisfied it is not a motivator anymore, and when one's need is satisfied, the one above it becomes the most proponent determinant of behaviour (Pardee, 1990). The Hierarchy of Needs is widely used in different types of research including organizational research (Deci & Richard, 1985).

2.1.1.2 Extrinsic Motivation

Extrinsic motivation is often seen as a less powerful, watered down version of intrinsic motivation. However, Self-Determination Theory proposes that there are various types of extrinsic motivation, some of which can act as a catalyst in the same way as intrinsic motivation (Deci & Ryan, 2000). Organismic Integration Theory (OIT), which is another subtheory of SDT, categorises extrinsic motivation depending on the varying degree of autonomy (Deci & Richard, 1985). OIT proposes that there is a large difference in outcomes between a student doing her homework because she is afraid of being grounded by her parents, and a student doing her homework because she believes it will be beneficial for her future career. Both of these students are doing their homework because of a separable consequence, i.e. because of an extrinsic motivator, but with a varying sense of autonomy. Figure 3 shows OIT's different stages of motivation, arranged from left to right with the least autonomous motivation to the far left, and the most autonomous motivation to the far right. Differences in attitudes and adjustment are associated with the different types of extrinsic motivation. For instance, it has been shown that the less autonomous a student feels, the less interest and effort he or she will exert (Ryan & Connell, 1989). Further studies have shown that extrinsic motivation at a more autonomous degree is associated with greater engagement, better performance and higher quality learning

(Miserandino, 1996; Grolnick & Ryan, 1987; Deci & Ryan, 2000). The same positive effects on the quality of the output can be observed in an organisational environment. Examples for extrinsic motivators in a work context are promised reward, deadlines, goals and surveillance (Amabile, 1993).

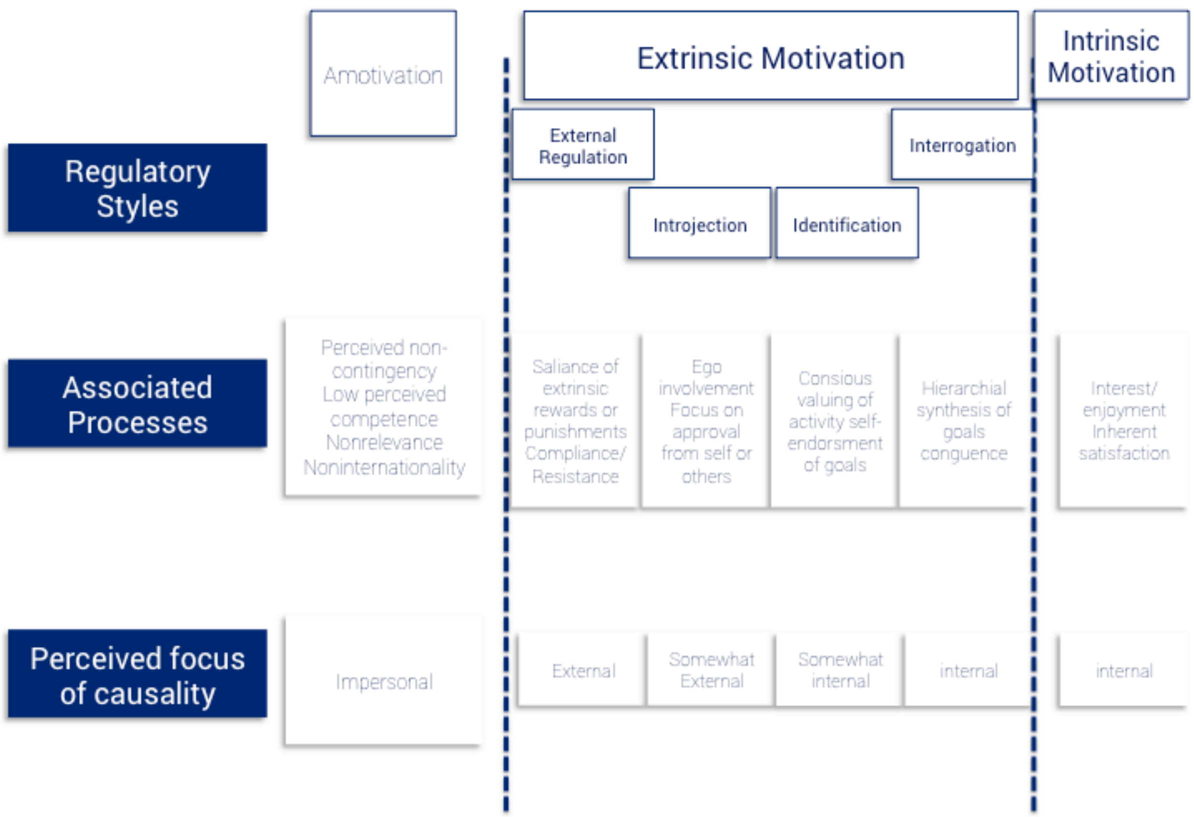

Figure 3: Stages of Motivation in Organismic Integration Theory (Deci & Richard, 1985)

The impact of extrinsic motivators on an individual's intrinsic motivation is debated. A meta-analysis by Deci, Koestner & Ryan (1999) establishes that extrinsic rewards contingent on an individual's performance, threats, deadlines, directives and competition all undermine an individual's intrinsic motivation. CET explains that this is because individuals regard these motivators as undermining their free will or autonomy. However, researchers also suggest that extrinsic motivators may have a reinforcing effect on intrinsic ones. Amabile (1993) for example argues that extrinsic motivators like project goals that increase an employee's focus on the nature of the task or rewards that involve more time or freedom to deal with exciting ideas enhance intrinsic motivation. Furthermore, as shown in Karl Dunckers candle problem (Duncker & Lees, 1945), extrinsic motivators such as monetary rewards can "crowd out" creative thinking. In the experiment researchers ask two groups of people to solve a task. One group is rewarded for the speed of completing the task the other is not. In this instance the group that is not rewarded completes the task faster on average then the group that is rewarded. Scientists suggest that the reason for this is that the introduction of monetary rewards can inhibit creative thinking, as it introduces such a strong incentive to preform that it blocks ideas i.e. the subjects become so stressed that they have a hard time thinking creatively (Pink, 2014).

Another well-used motivation model within management research is the Herzberg two-factor model (figure 4) (Herzberg, Mausner & Snyderman, 1959). In this model we can see several examples of extrinsic motivation, and how these can be analysed. He outlines satisfiers and dissatisfies or hygiene factors and motivators. The idea is that without the hygiene factors people are less motivated or become less satisfied with their work environment. The motivators or satisfiers on the other hand, can make employees more satisfied with their work environment (Pardee, 1990).

Satisfiers	Dissatisfiers
1. Achievement 2. Recognition 3. Work itself 4. Responsibility 5. Advancement 6. Growth	1. Company Policy 2. Supervision 3. Working conditions 4. Interpersonal relations 5. Salary 6. Status 7. Job security 8. Personal life

Figure 4: Herzberg's Two-Factor Theory

2.2 Possible Funding Sources

After having outlined the concept of motivation and how it relates to human capital and organisations in general, the context in which it is used in this thesis is introduce in the following section. In order for a company to be started and able to operate, financial capital is one of the essential resources. There are a number of different ways available for an entrepreneur to raise money. On a general level, the possible sources of financing can be divided into three groups - debt financing, equity financing and insider funding (figure 5) (Cassar, 2004; Söderblom, 2012).

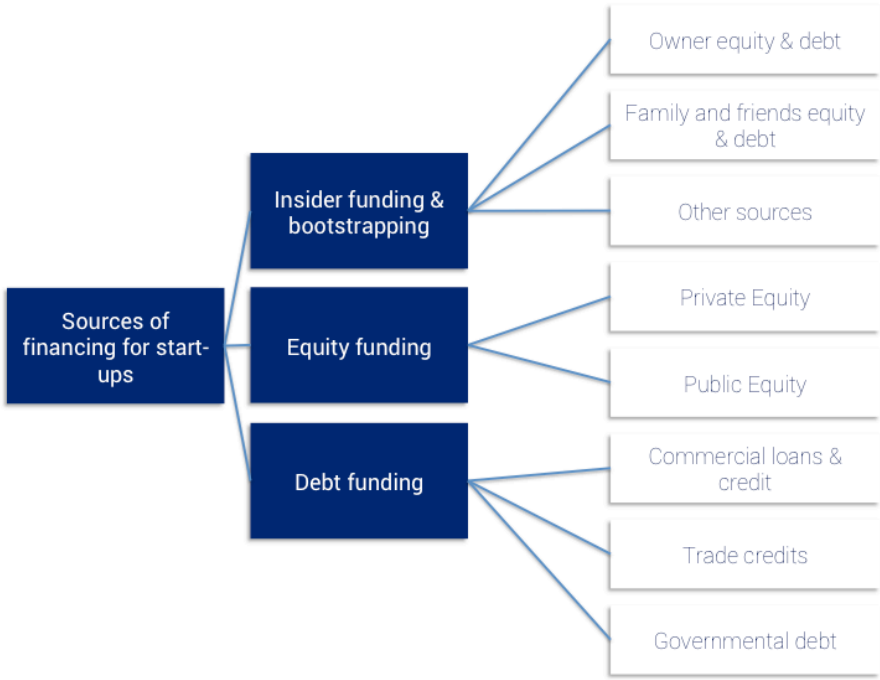

Figure 5: Possible sources of financing (Söderblom A. , 2012)

2.2.1 Characteristics of Funding Sources

The three different categories of funding sources have distinctive characteristics. In case of a debt investment, the investor provides a fixed amount of capital for a predetermined time period to a given interest rate. Since debt investors do not participate in an enterprise's success, they have a limited upside but can still lose their whole investment. The most typical sort of debt financing is a bank loan but it is also available from various other sources like the government, savings and loan institutions, finance companies, and other institutional lenders (e.g. insurance companies, pension funds). Debt lending can be done in form of cash flow financing and asset-based financing. In the first case, an investor lends money to a firm against the expectation of them being able to generate cash and pay back the loan. Asset-based financing refers to a loan, which is secured by a pledge or first line on specific assets (e.g. inventory, accounts receivable, equipment, real estate etc.). For the reason that cash flow financing is generally riskier, investors reduce their risk by demanding a covenant on the loan (e.g. minimum cash balances or limits on the company's debt/equity ratio). Furthermore, start-ups usually need to have an earnings history in order to obtain cash flow financing. Since new ventures only have a limited earnings record, it is often easier for them to obtain asset-based financing (Kerr & Nanda, 2014).

Equity investors on the other hand obtain a long-term ownership claim over the company they invest in. In that case, the investor limitlessly participates in the success of a company with his ownership stake in proportion to the company's value. This makes it more attractive for equity investors to invest in more risky projects. The most prominent sources of equity investments are venture capital firms (see section 2.3 for a thorough analysis) or business angels (Kerr & Nanda, 2014). Business angels are "high-net-worth individuals who typically invest in small, private firms." In contrast to venture capital firms, angel investors invest their own money and do not raise funds from institutional investors (Wong, Bhatia & Freeman, 2009).

"Insider funding refers to the capital provided by the owner/entrepreneur herself, either alone or in combination with family and friends" (Söderblom A. , 2012). The owner can provide capital in form of both, debt and equity. However, Robb & Robinson (2012) conclude from their research that owner debt only plays a minor role while a great proportion of new ventures rely on equity financing by the owner making it an important capital source for start-ups. Considering the financial support from other insiders (e.g. family, friends, spouses etc.), debt funding is more common than equity funding. However, the overall number of companies relying on funding from family and friends is much smaller than the one taking in owner's funding (ibid.).

In addition to the categorization above, there exist a number of other ways of financing that cannot be clearly assigned to one of the categories mentioned above but which are still worth mentioning for the sake of completeness. One example is financial bootstrapping. Thereby, entrepreneurs meet their capital needs without long-term financing from external sources or the owner. Ways to do this are for example speeding up invoicing, delaying payments to suppliers, withholding the manager's salary or sharing and borrowing resources from other businesses (Winborg & Landström, 2001). Furthermore, enabled through the technological progress, crowd funding has become another growing alternative to finance one's business. Crowd funding refers to an open call – usually through Internet platforms (e.g. Kickstarter, Indiegogo etc.) – for monetary resources. Thereby, the entrepreneur does not target a specific investor but rather a great number of smaller investors. The provision of capital occurs either in form of a donation or in exchange for the future product or some other form of reward (Belleflamme, Lambert, & Schwienbacher, 2014).

2.2.2 Availability of Funding Sources

New ventures not always have the opportunity to choose from which of the above-described sources they want to raise capital. The available possibilities for a company to finance its operations rather depend on prevalent information asymmetries and a company's financing life cycle (Berger & Udell, 1998). The information asymmetries can be explained by the principal-agent theory. This problem arises out of the different goals the owners and the managers of an organization might have. Since it will never be possible for the owners to fully control the managers, the problem manifests itself when the information about the managers is incomplete (Laffont & Martimort, 2009). In the context of an investment in a start-up the investor takes the role of the principal while the entrepreneur functions as the agent. Information asymmetries is an even greater issue when it comes to running a governmental venture capital fund since the principal-agent problem takes on a different dimension when handling tax money. The information asymmetries not only exist between the Swedish government – being the principal of the fund itself – and the managers of the fund but also between the Swedish tax payers as principals of the tax money and the government as the party managing it.

Building on the assumption that the firm (i.e. the entrepreneur) has information that its potential investors do not have, Myers and Majluf (1984) have developed the pecking-order theory of capital structure choice. This theory basically states that the prevalent information asymmetries concerning a company's on-going operations and its future outlooks lead to the fact that new incoming investors demand a higher rate of return on their investment than using existing internal funds. The higher the risk related to the differences in information, the higher the return on investment demanded by the respective investors. Therefore, the information asymmetry is a decisive determinant of the cost of capital resulting in the fact that entrepreneurs will prefer inside finance to debt, short-term debt over long-term debt and any debt over outside equity (Cassar, 2004; Myers & Majluf, 1984). The access to the public debt market facilitates this pecking order behavior. However, at a certain level of information asymmetry a company looses its access to the public debt market which limits the sources of financing to private debt and equity and results in a behavior not in line with the pecking order theory (Shen, 2014).

Detached from the effects of existing information assymetries, Berger and Udell (1998) argue that firms have a financial growth cycle in which the financial needs and the available funding sources change while a company grows, gets more experienced and the available information on the business increases (figure 6). Their theory suggests that young and small firms without any track record (i.e. start-ups) only have access to insider funding, angel investments, trade credits and short-term loans. As a firm increases in size and establishes a track record, other capital sources like venture capital, public equity and public debt become available. This financial growth cycle theory is one explanation why start-ups might not behave according to the pecking order theory.

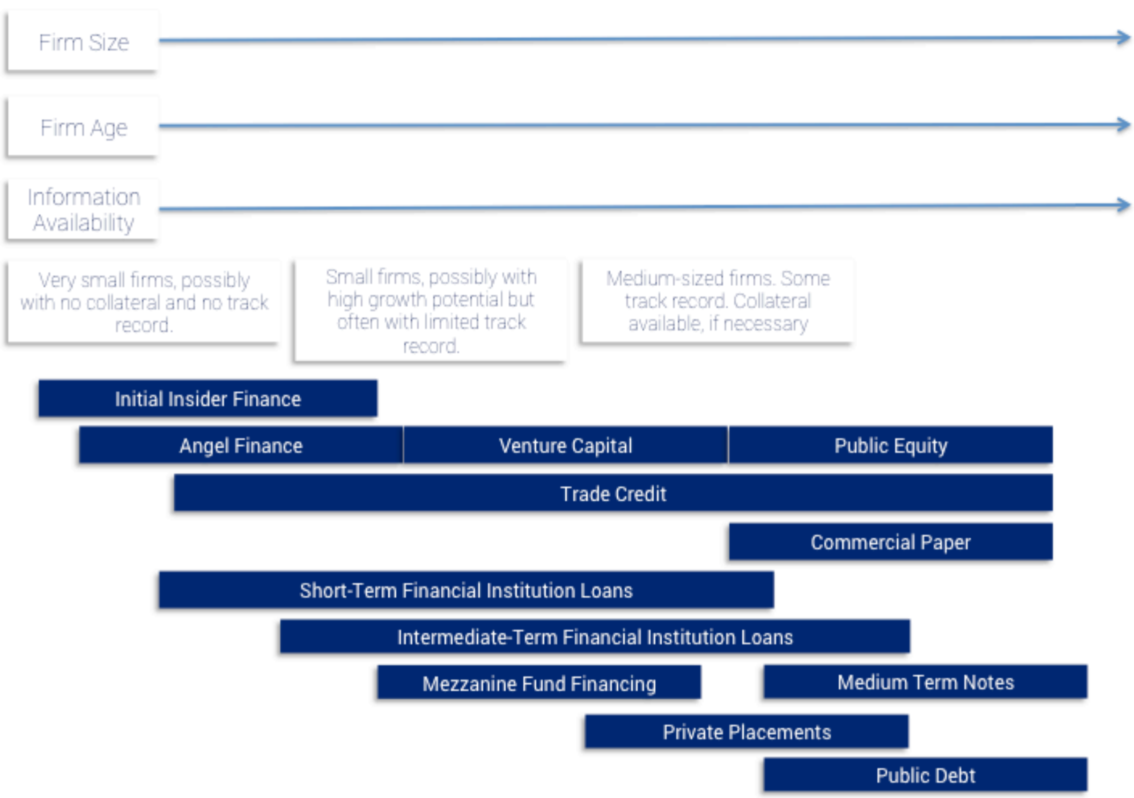

Figure 6: Available funding sources throughout a company's life cycle (Berger & Udell, 1998)

All in all, it is important to note that the different sources of financing for new start-ups are not mutually exclusive but might even complement each other. Research shows that entrepreneurs behave according to the pecking order theory in a way that they use internal sources of financing first. However, they do not behave in line with this theory when external funding is required since in that case they rather take equity investments than debt investments (Paul, Whittam, & Wyper, 2007). One possible reason for this is that availability of the various sources depends on information asymmetries, size, scale, demand for finance and asset structure and therefore also on a company's financing life cycle. For example low scalability of a business makes it less attractive for equity investors (e.g. venture capital firms) to invest, while debt investors are still willing to provide capital (Cassar G. , 2004).

2.3 Characteristics of Venture Capital

The way motivation and human capital relate to the organisation is discussed in the first section of the literature review. In the previous section the field of financing start-ups and the problems related to that are introduced, in order to provide a context for the venture capital organisation. In this section the venture capital organisation as such is described, and the characteristics of that specific organisation as well as the differences between the different types of VCs is described.

As mentioned above, venture capital is one possible source of external equity funding for a start-up. Venture capitalists are willing to invest into a new venture at an early stage where they are still exposed to high risks but also have a high growth and high return potential. They usually buy those equity stakes at a point when the start-up is still privately owned (Gompers & Lerner, 2010). Gompers & Lerner (2010) define venture capital "as independently managed, dedicated pools of capital that focus on equity or equity-linked investments in privately held, high-growth companies." Their preference of investing in scalable, high-growth companies makes them specialize on innovative firms that have the potential to either provide a higher quality product to an existing market and thereby disrupt the market or on companies that create a new market on their own. Furthermore, venture capital funds are usually not considered as being long-term investors but rather wish to exit after four to seven years, preferably when a company goes public (Schweinbacher, 2008). Nevertheless, venture capital has a sizeable effect on new business creation (Popov & Roosenboom, 2013). There is substantial support for the notion that venture capital is conducive to bringing new ideas and innovation to the market. If compared to some of the other forms of early stage funding in the market, venture capital fills an important function in satisfying the financial needs of start-ups (Popov & Roosenboom, 2013).

According to Söderblom (2010), a further characteristic of venture capital funds is that they are, like angel investors, considered to be “value added” investors. This refers to the fact that they, besides capital, also provide industry-specific knowledge and access to their networks. One main difference between those two investors is that business angels are usually privately organized while venture capital firms are institutionalized. Furthermore, angel investors invest their own money whereas venture capital funds raise money from their limited partners (i.e. institutional investors or wealthy individuals) to invest (Wong, Bhatia, & Freeman, 2009). However, entrepreneurs might rely on both ways to raise capital in which case angel investors often come in earlier in a company’s lifespan than venture capitalists do. Compared to the sources of debt financing (e.g. bank), the biggest difference is that venture capital firms provide the above-mentioned value-adding services (Da Rin, Hellmann & Puri, 2011; Chemmanur & Chen, 2006).

2.3.1 Types of Venture Capital

Venture capital firms are organized and governed in line with their respective ownership structure, which is seen to have some important effects on company performance (Da Rin, Hellmann, & Puri, 2011). According to the relevant literature, venture capital firms can be divided into four main types: the independent, the corporate (affiliated with a non-financial corporation), the bank controlled and the governmental venture capital firm, where the latter three categories are referred to as captive venture capital firms. Those are usually affected by the organisation owning them (Da Rin, Hellmann & Puri, 2011; Colombo, Cumming & Vismara, 2014; Chemmanur, Loutskin & Tian, 2014). Figure 7 shows a line-up of the different forms of venture capital firms.

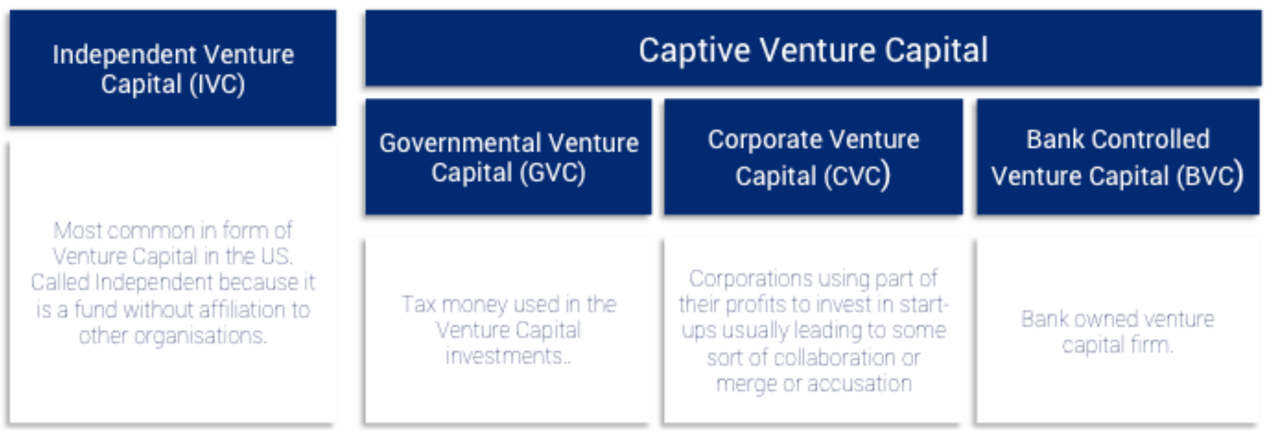

Figure 7: Types of venture capital firms

The independent VC firm has limited partners (usually institutions like pension funds etc.) providing money for their fund, which is managed and invested into new ventures by the venture capital firm. The most common set-up is a close-end fund that is dissolved after a predetermined timespan (typically 5-10 years) (Da Rin, Hellmann, & Puri, 2011).

The corporate venture capital firm is privately owned by a corporation. Similarly, the bank controlled venture capital firm is privately owned by a bank. Through this VC, the organisation behind it directly invests in another corporation or a start-up. This VC firm is described as a good way for larger corporations to be innovative without having to develop the necessary product or service themselves. It is an efficient mean to acquire innovative ideas in one's business (Ernst, Witt, & Brachtendorf, 2005).

The most distinct type of captive VC is the governmental one (GVC), as it displays some singular behaviour in terms of investment (Bertoni, Colombo, & Quas, 2015). The GVC – more common in Europe than the US – is typically under scrutiny because it is thought of as a controversial subject for the government to invest tax money directly into companies, large or small. The common idea behind the GVC is to try and fill the equity gap in the market and through this foster innovation. In addition to this, the GVCs have a strong signalling effect. An initial investment by a GVC often leads to subsequent investments by private VCs (Colombo M., Cumming, Douglas, & Vismara, 2014). This is due to the fact that the GVC in that case works as a reducer of information asymmetries between the non-public VC and the entrepreneur. By investing in a company the GVCs signal other investors that they place trust in that company (Lerner J. , 2002). The GVCs around the world are generally thought of as lacking in performance, however research does point out that this might be undeserved. The behaviour of GVCs is arguably different than the one of other VCs, including goals and human capital differences (Da Rin, Hellmann, & Puri, 2011) but the performance is not always worse (Colombo M., Cumming, Douglas, & Vismara, 2014).

Several papers have sought to find the effect of governmental venture capital on the performance and future funding of a new venture as well as the difference of the effects to a private venture capital firm. Brander, Du and Hellmann (2015) find that GVC's existence in a market usually correlates with more overall VC investments as well as with better exit outcomes, and is therefore deemed positive (Brander, Du, & Hellmann, 2015). On a company level, evidence shows that companies that are funded by both GVCs and PVCs obtain more funding in total than those only funded by PVCs and much more than those only funded by GVCs. Additionally, companies with mixed backing have higher exit rates than companies backed only by one source of venture capital. This effect can be largely explained by the higher total investment amounts. Overall, start-ups that only receive GVC funding are associated with weaker performance. It is argued that those companies, might not receive any funding at all if the GVCs would not invest in them (Brander, Du, & Hellmann, 2015). Furthermore, the difference in the offering of value adding activities between the GVC and the IVC (Independent VC) might also be an explanatory factor for the differing performance of new ventures. Research shows that the amount of value adding activities from IVCs is insignificantly higher than the one contributed by GVCs. However, the value adding activities are concentrated on different areas. Independent VC concentrate much more on implementing corporate governance systems, exchanging the management team as well as finding board members and have a higher focus on the exit compared to GVCs (Luukkonen, Deschryvere, & Bretoni, 2013).

While the investments from IVCs are foremost driven by the prospective financial success, the goal of the GVC is typically not exclusively to make as much money as possible, but to for example spread the investments throughout the country into underfinanced industries or socially underdeveloped areas in order to alleviate market imperfections. Thereby, they are often driven by social payoffs or public benefits like job creation or economic growth. This difference in goals between the GVC and the private VC is an obvious source of the difference in behaviour since it also leads to investments in different types of companies. Furthermore, it affects the design of the investment decision process of GVCs (Colombo, Cumming, & Vismara, 2014). Because of this, the difference in the design of the investment decision process and the various motivations leading to those differences are important area to do research in.

The following section is dedicated to a detailed theoretical outline of the investment decision process of a venture capital firm. These insights serve as a basis for the analysis of the findings. For the purpose of this paper, the different kinds of venture capital firms are referred to as private (i.e. corporate VC, bank controlled VC and independent VC) and governmental VCs instead of independent and captive venture capital firms.

2.3.2 The Process of a Venture Capital Firm

There exists an extensive amount of research on the steps and models that are involved in the process that leads to an investment conducted by a venture capital firm. Tyebjee and Bruno (1984) for example suggest a five-step model of a venture capitalist's activities (Clercq, Fried, Lehtonen, & Sapienza, 2006). In their model the activities start with the deal origination, which refers to the way new ventures attract the interest of a venture capital firm and are taken into consideration as a potential investment. In the screening phase, the investment opportunities are reduced to a manageable number of promising companies, which get evaluated further. During the third step, the deal evaluation, the remaining companies are subject to an in-depth assessment following criteria like perceived risk, expected return or the competency of the management team. The evaluation step results in the investment decision of the venture capitalist. Thereafter, the structuring phase deals with the negotiation of the terms according to which a deal should be carried out. The fifth and last step is concerned with the activities a venture capitalist carries out after the investment in a start-up in order to create value for it.

Similarly, Fried and Hisrich (1994) derive a model consisting of six stages leading to a VC's investment decision from their research (Bliss, 1999; Clercq, Fried, Lehtonen, & Sapienza, 2006). As shown in figure 8, this model involves the steps *I) origination, II) VC firm-specific screen, III) generic screen, IV) first-phase evaluation, V) second-phase evaluation and VI) closing*. At any of those stages, it is newly decided if the investment proposal proceeds to the next phase or if it gets rejected.

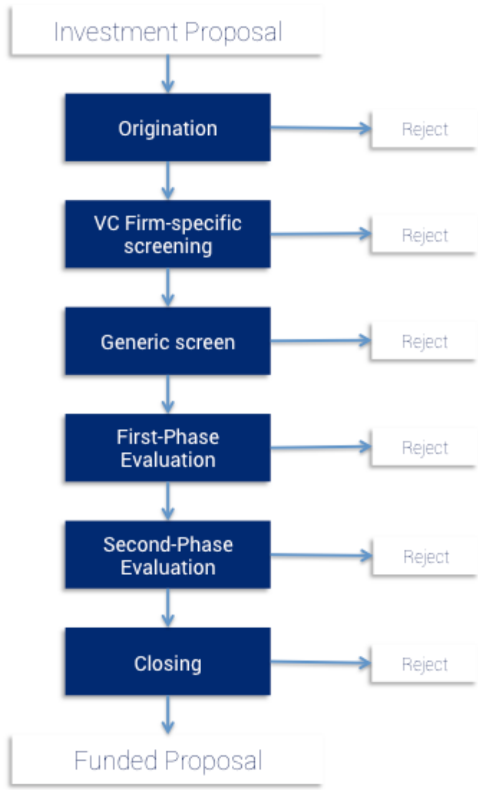

Figure 8: A VC's investment decision process (Fried & Hisrich, 1994)

The majority of the previous research takes very similar steps and content of a VC's activity into account. While the different models mostly start with the deal origination, the main distinction is that some end with the actual investment into a start-up, while others also take post-investment activities or even the exit stage into consideration. Since this thesis analyses the differences in factors affecting the process leading up to the actual investment, the model developed by Fried and Hisrich (1994) is argued to be the best suitable starting point. Therefore, this model is described in depth and combined with the results of other researchers below.

2.3.2.1 Origination

The origination stage describes how a VC becomes aware of a potential investment opportunity. In a market economy, there are three ways through which a VC can get introduced to potential new investments: *proactive applications from entrepreneurs, referrals by a third party and the active search for new deals.*

Cold calls from entrepreneurs refer to a situation where the entrepreneur is proactively applying for funding at the VC firm. Referrals by third parties can come from players within the VC industry, from previous investees, personal acquaintances, investment bankers or similar sources. The third way to source new investment opportunities is if the VC firm actively searches for potential companies. This can happen for example through an informal network or through taking part in conventions (Fried & Hisrich, 1994; Tyebjee & Bruno, 1984).

Generally, VCs make themselves known to entrepreneurs through industry directories or conventions. As a result they receive many deal suggestions from entrepreneurs applying for funding. However, they only invest in a small number of those unsolicited proposals. In fact, most of the ventures that ultimately get funded are referred to the VC's through their network. According to Fried and Hisrich (1994) the reason for this is two-folded: *I) there is a greater likelihood that referred deals pass the generic screen stage if the referrers judgement is trusted by the VC and II) the party referring a deal knows what sorts of investment a VC is interested in*.

2.3.2.2 VC firm-specific screen

This first screening is conducted on a very general level according to the VC's specific investment criteria regarding the size of the investment, the industry and market sector the venture is operating in, the geographic location of the venture and the stage of financing. The assessment usually only depends on a rather superficial glimpse at a start-up's business plan without any in-depth valuation. At this stage, the investment proposals that do not correspond with a venture capital firm's strategy and investment policy are discarded.

2.3.2.3 Generic screen

The generic screen involves the reading of the business plan. The start-ups are rejected or passed on in the process according to generic criteria in combination with a VC's previous knowledge relevant to the deal. The generic criteria Fried and Hisrich (1994) identify in their research can be divided into three categories (figure 9):

Figure 9: Criteria for generic screen (Fried & Hisrich, 1994)

The particularities as well as the relative importance for each criterion vary between different VCs. The goal of the two screening phases is to significantly reduce the number of proposals with a minimum investment of time.

2.3.2.4 First-phase evaluation

At this stage the VC starts to gather additional information about the start-up in order to determine if there is a serious interest in the deal. This gathering typically begins with meetings with the management team of the company and involves a number of other activities (figure 10). Therefore, this stage is associated with a significant investment of time and money. By carrying out the activities, the VC firm tries to get a feeling for the structure and pricing of the potential deal and to eliminate proposals that are not fundable before investing too much time.

Venture capitalists were asked: "Prior to funding an investment as lead investor, how often do you engage in the following activities ?"

ACTIVITY	HOW OFTEN (%)
Interview all members of management team	100
Tour facilities	100
Contact entrepreneur's former business associates	96
Contact existing outside investors	96
Contact current customers	93
Contact potential customers	90
Investigate market value of comparable companies	86
Have informal discussions with experts about the product	84
Conduct in-depth review of pro forma financials prepared by company	84
Contact competitors	71
Contact banker	62
Solicit the opinion of managers of some of your other portfolio companies	56
Contact suppliers	53
Solicit the opinion of other venture capital firms	52
Contact accountant	47
Contact attorney	44
Conduct in-depth library research	40
Secure formal technical study of product	36
Secure formal market research study	31

Figure 10: First-phase evaluation activities (Fried & Hisrich, 1994)

2.3.2.5 Second-phase evaluation

After progressing through the first evaluation stage, the proposal enters the second evaluation stage. During this phase, the evaluation activities continue. However, while in the previous evaluation phase the goal is to decide if there is a genuine interest in the investment opportunity, this second evaluation is more concerned with identifying the obstacles to the investment and how they can be removed.

2.3.2.6 Closing

At the last stage of a VC’s investment decision process, the details and the structure of the deal are finalized as well as the legal terms are negotiated. Furthermore, the documents are signed and the VC firm provides a check to the start-up. Although the VC firm as well as the entrepreneur invest a lot of time and money throughout the whole process, 20% of the companies reaching this final stage are not funded after all (Fried & Hisrich, 1994).

The outlined process that leads from many prospective start-ups to only a few which actually get funded after all can be thought of as a funnel where the number of companies decreases with every step since continuously some of them are rejected due to not meeting the criteria. In case a VC firm identifies a problem with a certain proposal it – besides rejecting it right away - has three different options to react:

- Further investigate the proposal
- Demand changes in the proposal
- Go ahead with the deal despite the concerns

While the number of ventures decreases with every step, the time spent on a specific proposal and the thoroughness of the analysis increase in the later stages (Fried & Hisrich, 1994).

2.4 Research Gap

Following from the analysis of the existing research, a clear theoretical gap is identified. As elaborated, there is a vast amount of research on private and governmental venture capital. Previous research in the field mostly concentrates on analysing the difference in performance between those two kinds of VCs and on the effects the different investors have on a start-up and its performance (Colombo, Cumming & Vismara, 2014; Brander, Egan & Hellman, 2008; Samulesson, Söderblom & Wiklund, 2015). Other researchers try to find the cause for the performance gap between governmental and private VCs. Thereby, a focal point is on the differing goals of public venture capital firms and how these goals relate to the post-investment behaviour of the firms, which subsequently affects the performance (Luukkonen, Deschryvere & Bretoni, 2013; Lerner J., 2009; Colombo, Cumming & Vismara, 2014). However, none of the reviewed publications concentrates on the correlation between goals and pre-investment behaviour i.e. the investment decision process. If the goals of a VC firm influence the post-investment behaviour, it is only reasonable to assume that they influence the investment decision process as well.

Furthermore, previous research identifies human capital as an important factor to consider in the VC organisation. The connection between an internal process and the people preforming that process is of evident importance. The main factor separating the employees of a GVC from the ones of a PVC is likely to be the way they are extrinsically motivated, as previous research proves that other human capital related factors are very similar in different VCs (Zarutskie, 2010). Since goals are one way of extrinsically motivating employees, there is also a clear link between motivation and human capital. The identified research gap relates to the influence that goals have on extrinsic motivation and how this in turn affects the behaviour of the employees performing the decision making process. Since the goals differ between the two types of organisations, PVC and GVC, a comparative study is conducted to analyse how the differences in employee motivation and investment goals between governmental and private venture capital firms affect the investment decision process.

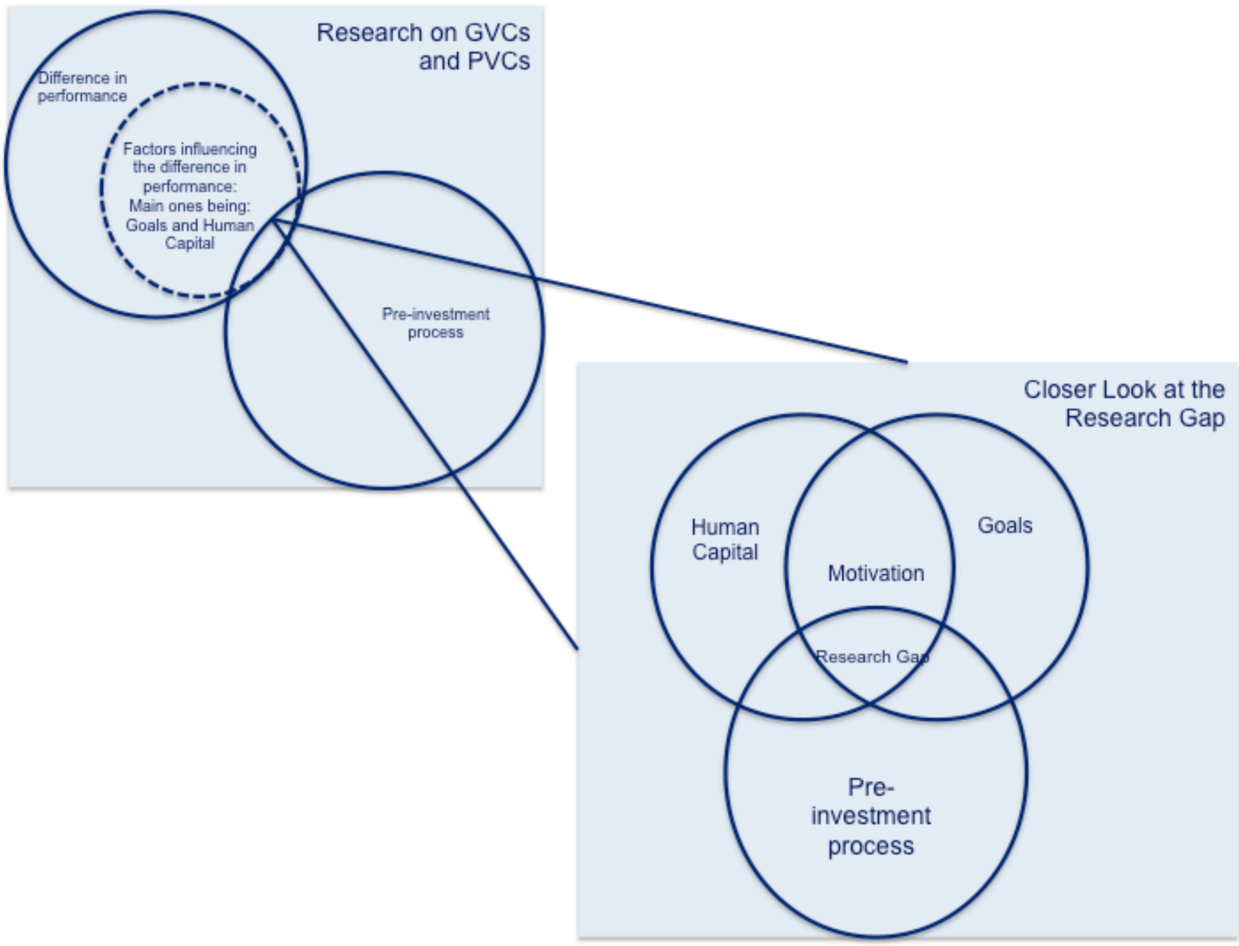

Figure 11: The research gap

2.5 Theoretical Framework

In order to facilitate the understanding of the reader and to address the research question in a structured way, the theoretical framework shown in figure 12 was developed. This framework aims at visualizing the factors that influence the investment decision process. The form of VC is at the top of our illustration. This refers to the organizational and ownership structure of the venture capital company i.e. governmental or private VC. The form of VC subsequently determines the goals a venture capital investor is pursuing and therefore, in turn influences the motivational factors and the human capital within the organization. Goals can be viewed as extrinsic motivation factors that influence most of the decisions made by the people within the organisation. The human capital in the organisation and their motivation influences how the investment decision process unfolds. For example, in a private VC where the goal is to maximize the return on investment and where employees are extrinsically motivated with monetary incentives, the employees execute the process in another way than in a governmental VC where goals and extrinsic incentives are different. According to this logic, the form of the organisation influences its goals, the motivation of its employees and finally the investment decision process. The structure of the different parts of this thesis follows this line of reasoning.

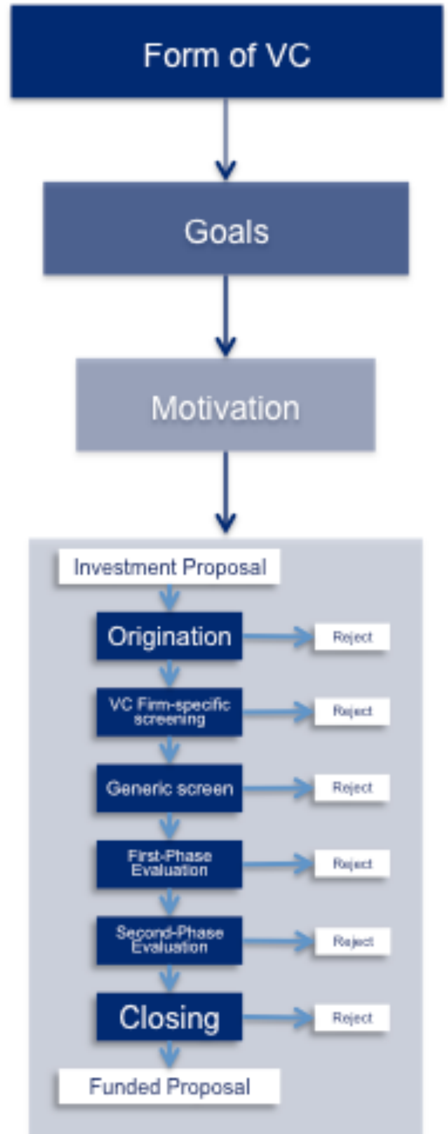

Figure 12: Theoretical Framework

3 Methodology

The following chapter guides the reader through the methodological approach and research design we applied. The aim of the research design, data collection and data analysis was to maximize the reliability and validity of our study.

3.1 Research Design and Methodological Fit

The study aims at providing insights into how human capital related differences in employee motivation, differing goals and process variations between the two distinctive fund types – a governmental fund and a private fund – affect the investment decision. For this purpose, the research design depicted in figure 13 was applied.

Figure 13: The research design

The starting point was an explorative review of the prevalent published literature within the field of interest. This theoretical review showed little research concerning the motivational factors that influence the decision process of a venture capital firm. Similarly, a lack of research on structural differences between an private and a governmental venture capital fund and its effect on the final investment decision has been discovered. As suggested by Edmondson and McManus (2007), a solely qualitative approach was applied in order to develop a theory in this under-researched field (Edmondson & McManus, 2007). Therefore, after doing a first literature review a small pre-study was conducted. It consisted of sending the interview questionnaire to the companies we questioned later on in order to get preliminary answers, feedback and a feeling of how the questions are perceived. These two steps served as a basis for a further, in-depth analysis of the existing literature and a descriptive field study composing of interviews. The interviews were guided by the feedback we have gotten from our pre-study as well as the (non-) existing literature and subsequently also influenced the type of the parallel consulted theory.

For the field study, a selection of the most relevant private players in Stockholm's venture capital industry, Creandum, Northzone, SEB Venture Capital and EQT Ventures. Additionally, the two existing governmentally funded VC firms Almi Invest and Industrifonden were questioned. In order to be able to draw a comprehensive picture of the process a VC applies before investing in a newly found company, the entrepreneurs' view was also included in the analysis. For this reason, a number of start-ups, which are located in Stockholm and have interacted with the above-mentioned VC companies were asked to elaborate on their experience. Those start-ups were Instabridge, Billhop and MatSmart. By incorporating those three different perspectives, we were able to get a holistic view on the investigated subject and arrive at our theoretical contribution to the field.

The whole process consisted of both, elements from a deductive approach when analysing what the general theory suggests for individual cases of the topic as well as elements from an inductive approach when inferring general applicable rules from our specific cases (i.e. the interviews). Scholars describe such a research approach as abduction (Arbnor & Bjerke, 2009).

3.1.1 Theoretical Research

The literature research started with a recommendation from Mikael Samuelsson, supervising this thesis, to read one of his articles (Söderblom, Samulesson, Wiklund, & Sandberg, 2015), which gave a good introduction to this field and the related, existing research. The references in that article also provided more pathways to follow and led into the particular research gap.

Once the research gap was discovered, we conducted an initial general search for publications concerning the venture capital industry on online databases like EBSCO, Google Scholar and ScienceDirect using general keywords related to the topic (e.g. venture capital, venture capital investment process etc.). The relevance of the articles picked for further investigation from this extensive list of results was ensured by taking the ones that were peer reviewed and matched closest with the decided field of research. Additional selection criteria for the articles picked also included the geographical area they focused on as well as similarities of the economic environment to the Swedish market. Articles solely examining the VC industry in emerging countries for instance were excluded, as the market forces are notoriously different from the ones in a developed market economy like the Swedish one. Since this thesis concentrates on the managerial aspects of the investment process rather than the financial ones, the articles examining VC from a management and organisational perspective were included, while research solely focusing on a financial perspective was not considered. Furthermore, the final bibliography represents a mix of the most recently published theory with relevant older ones containing the pioneering work on the investment process models. The result was a good overview on the findings in the field.

Besides the venture capital industry, motivational theories were also successfully searched for on the above-mentioned databases. The previous research in this area considered for the theoretical section of this thesis comes mainly from two different research fields: *I) management and II) psychology*. The literature from the management field mainly dealt with factors affecting the motivation of employees in a company. Since many of those articles are based on psychological research as well as for the reason that we wanted to discover how people are motivated on a more general level, it was considered necessary to also incorporate psychological papers that are not related to the work context. The result was a list of theories derived from experiments and observations in many different contexts, which was even more extensive than the one on the venture capital industry. Due to the vast amount of literature on motivation we were forced to concentrate on only a few specific models. After reviewing a number of articles we decided to divide motivation into intrinsic and extrinsic motivation and combine each of the two categories with the most reoccurring models of the literature. Thereby, an understandable structure as well as a comprehensive view on how people are motivated was ensured without confusing the reader by incorporating and analysing too many different theories on motivation.

The insights gained from this extensive literature analysis served as a basis for the interview structure and questions for the conducted field study.

3.1.2 Pre-study

After designing the interview guidelines according to the insights gained through the theoretical research, we conducted a test round with representatives of some of the VC companies we included in our main study. Therefore, we sent our questionnaire via e-mail to the person who also coordinated our interviews (i.e. administrative staff) at Creandum, Northzone and Almi Invest. The goal of this was to get feedback on the relevance of our topic as well as to get a feeling of how the questions are perceived and to get input on how to improve them. This was important due to the fact that we only had a limited number of interviews as well as a limited amount of available time for each interview. The result was that we could perfect our interview structure and were prepared in the best possible way for the meetings. Subsequently we were able to make the most out of it.

3.1.3 Field Study: Interviews

We chose to conduct personal in-depth interviews with representatives from private venture capital firms, from governmentally funded venture capital firms as well as with entrepreneurs who have been funded by either one of them or both. Thereby, we were able to take a holistic range of different perspectives into account for this study.

The interviews were conducted as semi-structured interviews, which is a non-standardized form of an interview often used for qualitative analysis (Kajornboon, 2005). Therefore, we prepared interview guidelines covering the most important issues and questions but still stayed flexible enough during the interviews to change the order of the questions and ask additional or other questions depending on the direction of the interview and previous answers. The advantage of semi-structured interviews was that we, as researchers, were able to prompt and probe deeper into the given situation (ibid.) and at the same time to keep the integrity of the answers by not "leading" the interviewee in his or her thoughts or prompt the answers in a way that would impair the honesty and authenticity of the responses.

3.1.3.1 Choice of Organizations

Interviews were conducted with representatives of private as well as governmental VCs and entrepreneurs. The criteria on which the representatives of the respective categories have been chosen are outlined below.

Private Venture Capital Firms

Throughout the research process, we conducted interviews with four representatives of as many private venture capital firms. Since the research done for this thesis solely investigated the prevalent behaviour patterns in the Swedish market, the firms were chosen according to two criteria: they had to be based in Sweden and they had to have made investments in start-ups incorporated in Sweden. The compliance with these two criteria was ensured by conducting a background check of potential companies on the Internet, where the location of the headquarter as well as information about the respective current portfolio companies was readily available. Although we actively picked the companies, it should be noted that, by limiting the scope to the Swedish market, a self-selection took place when it comes to the choice of private VC firms included in this study. This is due to the fact that the Swedish market is quite small with only a few big players actively involved.

As a result of those facts, we sent out inquiries for interviews to Creandum, Northzone, SEB Venture Capital and EQT Ventures, which all agreed on meeting us. Therefore, this sample of firms consists of three companies being in business for 13 years or longer and one company that only recently started in early 2016. Thereby, both firms with a lot of experience, long established processes and structures as well as one firm that designed its processes only recently were considered. When it comes to the representatives of those companies, we asked to and were also able to speak to people who were actively involved in and had a say in the investment decision process. Therefore, the interviewees typically held high positions in their company like partner, investment manager or fund manager.

Governmentally Funded Venture Capital Firms

For this thesis Industrifonden and Almi Invest were interviewed as representatives of governmentally funded venture capital firms. We met employees of both companies for an interview. Although Industrifonden is not operated by the government and does not get any new money from the government, it is still considered to be a governmental VC. The reasons for this are that Industrifonden was started with tax money only as well as is pursuing a vision determined by the government. Almi Invest has independently operating offices in different regions of Sweden. For reasons of geographical proximity as well as the assumption that the structures and processes of the different offices are very similar, we chose to conduct the interview with a representative of their Stockholm branch only.

As with the interview partner of the independent VCs, we asked to and were also able to speak to people who were actively involved in and had a say in the investment decision process. Therefore, the interviewees typically held high positions in their company like investment manager or fund manager.

Entrepreneurs

In order to fully understand the process, but also to get a validation of the answers given by the investors, three entrepreneurial companies (i.e. Instabridge, Billhop and MatSmart) were questioned about their experience during the process that led to their funding from a governmental VC, a private VC or from both. These three companies where picked because of their connection to the VC companies interviewed, which is relevant to get a deeper understanding of the investors' process. The interviews where used as a mechanism to get a more objective view of the process, from a party that has no "stake" in the outcome of this research.

3.1.3.2 Data Collection and Documentation

Patrick and James (2004) suggest several methods for data collection in studies on the process tracing e.g. video recordings, interviews or observations. Given our time constraint for this thesis, observing or recording the process leading to an investment decision was no possibility. To get an impression on the characteristics of the whole process and the factors influencing the final investment decision, interviews with the relevant actors working with the process have been seen as the ideal medium to gather data. Therefore, semi structured interviews have been the main source of data collection during the field study. The interviews have been conducted in the daily working environment of the interviewees at the offices of the respective companies. They have been recorded and notes have been taken throughout the interviews to ensure not to miss anything. For this reason, we have always been two people at the interviews with clearly defined tasks: one was always focused on the recording as well as note-taking without actually interacting with the interviewee, while the other concentrated solely on conducting the actual interview.

3.2 Data Analysis

The data analysis is based on the coding of the statements of the interviewees as a way of presenting and organizing the content of the interviews. Coding is essential to deduct new theories from qualitative data and is in this context defined as "the analytic process through which data are fractured, conceptualized and integrated to form theory" (Strauss & Corbin, 1990, p. 3). This procedure of coding was divided into two steps. At first, the essential statements from the responses to each question of the interviews have been identified. Thereafter, we decided on categories according to which the identified statements could be allocated as well as named the categories in a descriptive way to indicate the character of the statements subsumed under each category. Segmenting the responses of the interviews in this way allowed us to assess the importance of the different categories by counting the statements allocated in the respective classes. Although we tried to be as objective as possible when it comes to setting up the categories, it is important to consider that there is no totally objective, definitive correct set of categories but that it rather depends on our subjective assessment. In order to increase the objectivity, each of us conducted the identification and categorization of the relevant statements individually before we combined our findings and decided on the final categories based on the congruency of the individual results (Gillham, 2005, p. 134-139). For the analysis we not only categorized the statements according to their content but also divided them into three main groups depending who made the statements i.e. private venture capital firm, governmental venture capital firm and entrepreneur.

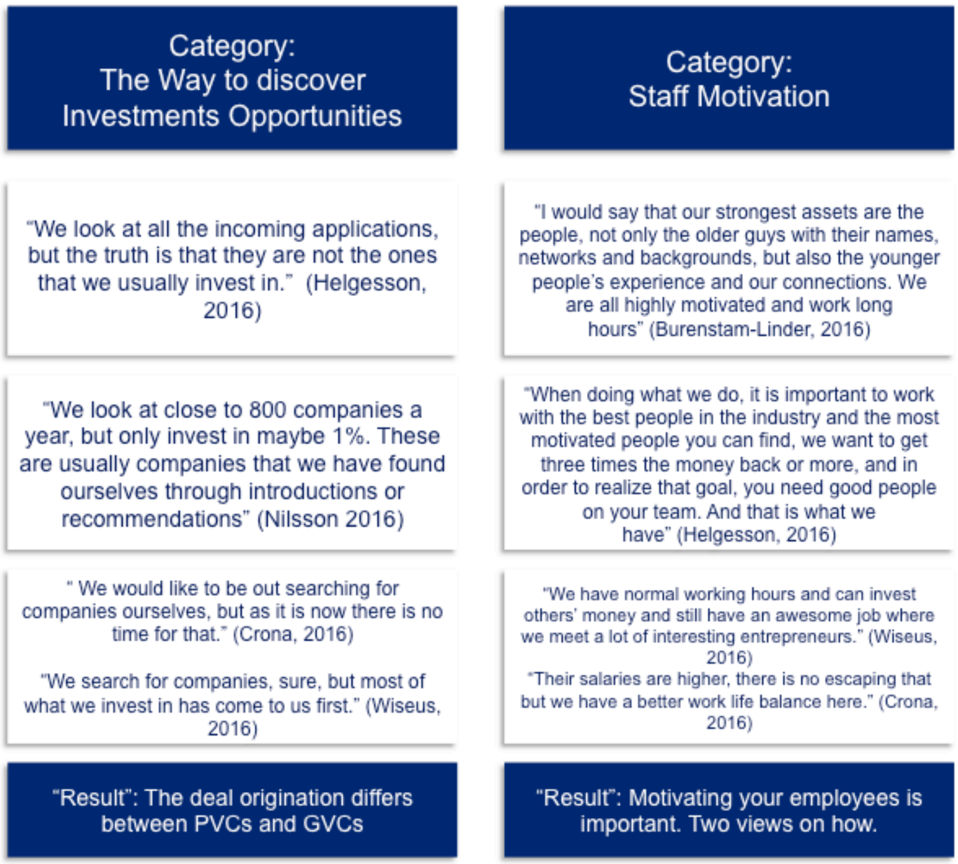

Figure 14: Example of deriving the categories from the statements

3.2.1 Data Quality

So far, researchers have not agreed on universal criteria to assess the quality of qualitative data. One reason for this is that researchers conducting qualitative research may apply a selective process, which refers to the fact that they only take statements into account, which they believe display the studied phenomenon the best. According to the literature, there generally exist two alternatives for assessing qualitative research. Either the classical criteria that are also used for assessing quantitative research (i.e. reliability, validity and objectivity) are applied or new criteria, specifically tailored to qualitative research (e.g. trustworthiness, credibility, dependability) are used (Flick, 2009, p. 384-385). Since there is no general agreement amongst scholars on the specific criteria for the quality of qualitative research, we decided to apply the classical criteria to our data.

3.2.1.1 Reliability

Reliability measures the extent to which a study can be replicated. If a study has a high reliability this refers to the fact that any researcher using the same methods also obtains the same results in comparison to the original study (LeCompte & Goetz, 1982). According to Flick (2009, p. 386), the reliability of qualitative data can be increased through a detailed documentation of the research process, by applying transcription rules, by checking the interview questions through conducting test interviews or by participating in interview training.

To account for reliability, we recorded the observations and took notes, rather than to analyse the data solely based on memory. In the framework of this study, we also tried to maximize reliability through standardizing the interview guide as well as through unifying the way notes were taken and interviews were transcribed. Furthermore, the detailed outline of the research process in this thesis is an attempt to increase the reliability of the results.

3.2.1.2 Validity

In conducting research, validity refers to the question if researchers actually see what they think they see. In this context, there exist three different kinds of errors possibly impairing the validity: seeing a phenomenon where there is none (type 1 error), rejecting a correctly observed phenomenon (type 2 error) and asking the wrong questions (type 3 error) (Kirk & Miller, 1986). Therefore, validity can be also defined as the accuracy and suitability of the measurement or the measurement device. A significant problem when assessing the validity of a qualitative research is how to specify the link between the relations that are studied and the version of them presented by the researcher. Therefore, both the production of data and the presentation of the phenomenon are important (Flick, 2009, p. 387-388).

Considering the data gathered from interviews, validity relates to the degree of authenticity of the statements of the interviewee. The authenticity in the production of data is maximized if the interviewees had no reason to consciously or unconsciously construct a biased version of reality and if they could tell their stories with a minimum of interventions by the researcher. To improve validity, the researcher has to analyse the interview situation for any indication of such deformations and their causes. In case such inconsistencies are identified, one has to think about how they have to be taken into account in the interpretation of the data (Flick, 2009, p. 388).

To increase the validity of our data, we posed open, neutral questions and gave the interviewees as much time to respond as they needed without any intervention from us. Furthermore, we did not share any results of previous interviews in order to not influence the person who is being interviewed and prevent them from giving biased answers. Nevertheless, it was hardly possible to eliminate all possible sources impairing validity. For instance it is reasonable to assume that most people questioned in this study wanted to portray themselves and their companies as favourably as possible. Furthermore, all the interviews were conducted in English, which was neither the mother tongue of the interviewers nor of the interviewees. Therefore, certain aspects might have been lost in translation. However, since all parties involved in the interviews were fluent in English, those effects are expected to be minor ones, and therefore have not been accounted for in the analysis.

3.2.1.3 Objectivity

The third classical criterion for data quality mentioned in the literature is objectivity. When it comes to the objectivity of the results, one needs to be concerned with the way the data is interpreted since it might be interpreted in different ways by different people. A high degree of objectivity is given when several independent researchers analyse the same data and arrive at the same conclusions (Flick, 2009, p. 391). By at first independently analysing and interpreting the transcripts of our interviews and later discussing our findings amongst ourselves as well as presenting the findings to independent parties such as our supervisor, we tried to avoid any negative impact on objectivity.

4 Empirics

In the following section the findings from the interviews are presented. The reader is introduced to the major private Swedish venture capital firms, Almi Invest, Industrifonden (i.e. the Swedish governmental VC firms) and a number of entrepreneurs. Through outlining the from the interviews gathered data a comprehensive view on their opinion and experiences on processes, motivational factors and other success factors is provided.

4.1 Interviews

For each category of interview partners a number of superordinate themes were identified as a result of the coding of the interviews.

4.1.1 Private Venture Capital Firms

When analysing the statements of the interviewees representing the private venture capital firms, two constantly reoccurring themes were identified: *the way how they discover investment opportunities* and the importance of *staff motivation*.

4.1.1.1 The Way to Discover Investment Opportunities

All of the interview subjects stated that they have seen a huge increase in interest for start-ups and in the need for and the availability of capital in the market within the last couple of years. For example, when an article about EQT Ventures was published in the newspaper, they received almost 500 spontaneous applications of aspiring entrepreneurs during the course of two months although they had not officially launched at that time. The sheer volume of applications is daunting, and the quality is very diverse. However, according to the SEB Venture Capital's head David Sonnek, one can see the first signs of a market decline, which is why he believes that in two or three years there will be a significant drop in activities.

From the statements it became clear that there is a huge number of entrepreneurs applying for funding at the moment. Since they are very busy, the VCs usually only superficially take a look at the applications and claim that they hardly invest in firms applying for money.

"*We look at all the incoming applications, but the truth is that they are not the ones that we usually invest in."* (Helgesson, 2016)

Instead it is a very non-transparent process of networking and searching for the right ideas. Most deals are done with companies that the VCs have "found" themselves rather than with entrepreneurs who approached them.

"We find companies everywhere from recommendations, other portfolio companies, newspapers, events, contacts and networking." (Nilsson, 2016)

Furthermore, the representatives of the firms all state that they are much more likely to invest in a company where they know someone. This becomes obvious when talking to EQT Ventures, the newest actor in the Swedish start-up financing scene. Out of the five companies that they have made deals with since they have started investing this spring, none has come from the deal flow coming in, but all of them are run by people that one or more members of the investment team have known before. The reason for this is the human factor. One just feels more comfortable investing in someone or something that one knows.

SEB Venture Capital is an outlier to this. Sonnek explains that they actually do not go out and "find" the ideas themselves. Instead he states that it is a process of mutual networking that brings in new deals to the fund. They find us and we find them. However, he is also convinced that only sending in an application has never lead to an investment.

When describing the process of finding investment opportunities, the investors say it is usually themselves or someone on their team who stumbles upon a great idea and makes an initial contact to get to know the entrepreneur. Only after a courting period, which might last years, a deeper analysis of the venture might take place and money might switch bank accounts.

4.1.1.2 Staff Motivation

"*When doing what we do, it is important to work with the best people in the industry and the most motivated people you can find, we want to get three times the money back or more, and in order to realize that goal, you need good people on your team. And that is what we have.*"

(Helgesson, 2016)

The private VCs all claim that they have the very best, most experienced and most motivated people working in the industry on their team. This includes on the one hand the people with the most relevant experience – often from founding a start-up themselves – and on the other hand people with different types of experience and education complementing each other. The amount of motivation shows itself in the willingness to work very hard and long hours if necessary.

"I would say that our strongest assets are the people, not only the older guys with their names, networks and backgrounds, but also the younger people's experience and our connections. We are all highly motivated and work long hours." (Burenstam-Linder, 2016)

These people are primarily motivated by the nature of their jobs, and the prospect of making a lot of money for the company as well as for themselves. The money as an extrinsic incentive is an important part when it comes to the motivation of the people. They get a high base salary, bonuses and often have stakes in the funds they manage. Another aspect of the motivation is that employees at private venture capital firms often have a background in entrepreneurship and therefore especially enjoy the type of work that they are doing. When asked how the background of the people that they work with helps them, Burenstam-Linder explains that venture capital is a "people sport" and knowing people in the industry is not just good, it is pivotal.

Another observation is that the backgrounds and experiences are the same for most of the people in the industry. The people interviewed all have a higher degree within business or engineering, have all worked in start-ups themselves, and afterwards gone into the financing of start-ups.

Making money, but also the nature of their work motivates them. They all explain that they get to meet entrepreneurs, companies and ideas that they would have never had the opportunity to meet if they would not have joined a venture capital firm.

Except SEB Venture Capital, all of the PVCs in the sample had closed-end fund structures. They also had a different salary structure, with bonuses but no ownership in the fund itself. This makes SEB Venture Capital an outlier. They are also a captured venture capital fund, which could be part of the reason why they where different. This is not unique for our sample however, as EQT Ventures is a captured fund as well.

4.1.2 Governmental Venture Capital Firms

When analysing the statements of the interviewees representing the governmental venture capital firms, three constantly reoccurring themes were identified: *the way how they discover investment opportunities, alternative ways to incentivize employees* and the *existing investment restrictions*.

4.1.2.1 The Way to Discover Investment Opportunities

The GVCs in Stockholm, Almi Invest and Industrifonden have offices right next to each other, in the same building, but apart from that they are completely different organisations with very different organisational structures. There are a few similarities however. One of the things is how they view the way they find companies to invest in. Since a great number of entrepreneurs approach the two of them (e.g. circa 400/year for Almi Invest) to pitch their ideas and ask for funding, none of the VCs have to proactively search for companies to invest in. But as we discovered in the PVC's case, a lot of them do anyway. Almi Invest and Industrifonden are similar in that they tell us that they do not actively search for investment opportunities.

" We would like to be out searching for companies ourselves, but as it is now there is no time for that." (Crona, 2016)

It is time consuming to deal with all the incoming proposals. Since the GVCs have the goal of educating the market, they perceive it as their responsibility to respond to all incoming funding inquiries and subsequently invest a lot of time and capacity in handling all the requests. Therefore, they do not have time to go out and actively search for companies. Both of the organisations mention how much time is spent on being cordial to people applying for funding, and making sure to take their responsibility as an investor and help the entrepreneurs.

"It is important to be a "polite" investor, or you might be left out of the consideration in the future." (Wiseus, 2016)

4.1.2.2 Alternative Ways to Incentivize Employees

According to the interviews, the motivation of people working at the governmental VC firms is quite different from the one of employees of private firms. While, as elaborated above, money plays a major role in private VC firms, it is far less important in governmental ones. A GVC rather motivates its employees by offering an as exciting job as the private firms but with fewer working hours and subsequently a better work-life balance.

"We have normal working hours and can invest others' money and still have an awesome job where we meet a lot of interesting entrepreneurs." (Wiseus, 2016)

Work life balance is an important issue for the employees at Almi invest.

"The salaries are higher in the private sector, there is no escaping that but we have a better work life balance here." (Crona, 2016)

The interview subjects also stressed that they enjoy feeling that they help the Swedish economy to prosper, by supporting innovative entrepreneurs.

4.1.2.3 Existing Investment Restrictions

On the financial side, Almi Invest has the goal to keep the capital intact. So far it is too early to evaluate their investments since only a few of the companies they have invested in have been sold. However, in order to reach their goal, Almi Invest aims at having a high risk - high return portfolio where they expect a great number of companies to go bankrupt and a few to generate a very high return. Industrifonden is an evergreen fund, which means that there is no new capital coming in. Their capital was provided by the government in 1979 and has quadrupled from 1 billion SEK to 4 billion SEK since. The difference between the two organizations also lies in the open-end and closed-end nature of their fund structures respectively. Being an evergreen fund implies that Industrifonden will never close the fund, and realize the capital. Instead they are flexible considering the investment's time horizon. Almi Invest on the other hand is a closed-end fund, meaning that they have a predetermined time horizon on their investments, and a fixed exit date to sell their shares. Another difference lies in the ownership structure of the two organisations, Almi Invest is a captured GVC, meaning that their owner i.e. the Swedish government has influence over their decisions and goals, while Industrifonden is as autonomous as a GVC can be because of the nature of their organizational form.

Normally, a VC tries to make money, and be responsible towards their investors. But as a governmentally funded fund, such as Almi Invest, one must not crowd-out money from private investors and one is therefore also not permitted to compete with investors from the private sector. Furthermore, Almi Invest can at the most provide 50% of the money raised in a given investment round and always need a co-investor from the private sector[2]. In most cases Almi Invest provides the remainder of the money of an investment round. Bringing in an investor from the private sector guarantees that the investment is made on market terms. The result of these requirements is that Almi Invest cannot invest in any company they want but rather can choose only among certain companies fulfilling those conditions. These restrictions inhibit some investments that Almi Invest could have done in the past. Industrifonden have no such restrictions, but a vision and other rules to adhere too. For instance one of their visions is that they make investments in the best interest for Sweden and to promote innovation.

The process is the same for the two GVCs. It comprises of three steps (Figure 15): *I) analysis, II) negotiation* and *III) due diligence.*

[2] Usually this is either an angel investor or someone who has already invested in the company in an earlier round.

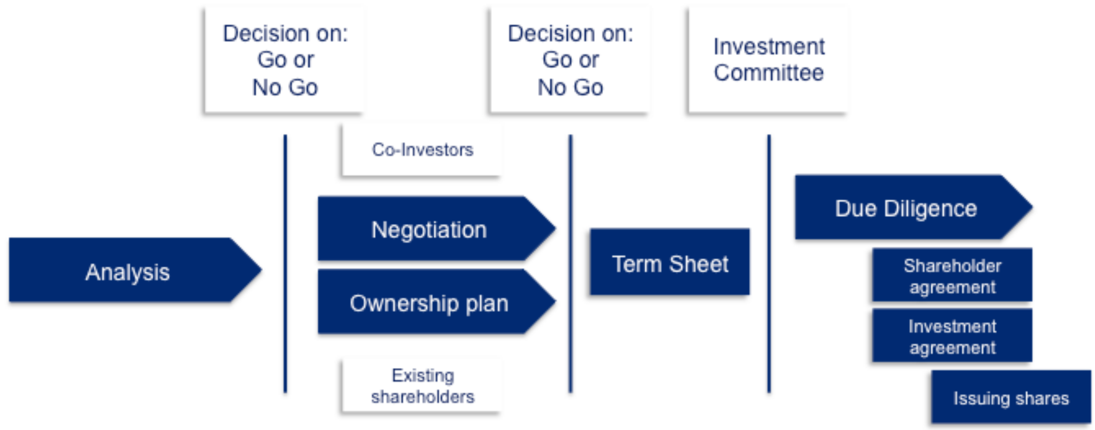

Figure 15: Investment decision process at Almi Invest (Crona, 2016)

During the analysis, their team of six investment managers makes an in-depth assessment of one company per week while discussing around 15 additional companies in a more superficial way in order to keep track of them. After profoundly analysing a company, the investment analysts all vote on the companies. This voting serves as the first go/no-go criterion.

The negotiation phase is devoted to negotiating and agreeing on the terms of the investment (e.g. board composition, valuation etc.) with the entrepreneurs as well as with the co-investors. Furthermore, Almi Invest's investment analysts discuss the resulting investment opportunity and present it to the investment committee[3]. This committee meets once a month and makes the formal investment decision.

The last step before the investment in a start-up is placed is to conduct a due diligence. This is usually a very simple process and only focuses on legal issues. The whole process from the point

[3] The investment committee is composed of anonymous people in order to not open-up any back channels.

where a company is closely analysed up to the actual investment takes about four to ten weeks, depending mainly on the meetings of the investment committee. Of the approximately 400 companies Almi Invest gets in touch with per year, they invest in ten.

4.1.3 Entrepreneurs

When analysing the statements of the interviewed entrepreneurs it was decided to subsume the them in one category named *the other side of the story.* The reason for this is that the whole point of questioning the entrepreneurs is to compare their statements to the ones of the different VCs to get a more objective ground for the analysis.

4.1.3.1 The other side of the story

The entrepreneurs’ view of the investment decision process is different, and usually less formal than the process presented by the investors. It becomes clear from talking to the Instabridge and MatSmart founders as well as one of the Billhop partners that networking is an important part of the process when getting investments. They are all honest about the fact that they talked to many investors, foreign and domestic, before they got any money.

The process they describe starts with a meeting in a casual setting or at a networking event. After this meeting, they had a long period of getting to know each other. Agelvik explained their process by first saying that he has probably met all the relevant investors in Europe and quite a few in the US. And that current investor, Creandum, did not want to give them any money at first. He thinks that it was “FOMO” or fear of missing out that finally got them to invest in the company's A-round of financing. Their courtship with Creandum lasted for a long while before money exchanged hands. In his opinion none of their investors would have given them money before he got to know them.

"Just sending in an application or presenting a PowerPoint would not have worked." (Agelvik, 2016)

Similarly, Andreescu explains that when they found investors it was through networking and events, rather than applying. Their introduction to Almi Invest took place at the Nordic Tech Meetup. MatSart founder Karl Anderson tells a similar story, it started with networking – it progressed from there. Billhop investors are both private and governmental players. Andreescu's opinion is that there are both differences and similarities between the two, but also that there are benefits to the differences. For example, Almi Invest, being a governmental investor signals the legitimacy of their business to customers and potential new investors. Operating in the financial industry, this is a decisive factor for Billhop.

"The investors from the government have a different point of view, it is often a good change of pace, they let us do things that might not immediately lead to more money for instance but that builds the company. It is also a good source of legitimacy for us, to have the Swedish Government as an investor. It makes us reliable." (Andreescu, 2016)

4.2 Summary of the Empirical Findings

In discussing the process with the investors from the PVCs as well as the GVCs we find subtle differences. The PVCs claim that they usually find the investment opportunities themselves, through using their network and meeting people at events. The GVC representatives on the other hand claim that all of their investments are a result of applications sent through official channels. In this case we have a contradicting story from the investee company, Billhop, who state that they have never sent an application to Almi Invest. All of their money in both of their investment rounds is a result of networking and meeting at different events. Sonnek from SEB Venture Capital points out that the deal origination is not a linear process. There rather is an element of networking that makes it hard to pin point exactly who finds whom and when.

When looking into the portfolio companies of the interview subjects one finds striking similarities in the investments. There are many examples of investments into the same companies. Fishbrain, Spotify, Tobii, iZettle, Footway and Qapital are only a few examples of companies that have been invested in by more than one of our interview subjects. This overlap is especially prominent in the PVCs but can also be found in the GVCs.

The gained insights show that venture capital is heavy in human capital. All of the interview subjects have pointed to the importance of their networks. It is also clear that all of the VC firms are dealing with a lot of deal flow – hundreds of applications a year. These are dealt with in different ways. The PVCs look casually at most of them, while the GVCs take every single one seriously. The employees at the two types of organizations are not very different. They have backgrounds in similar fields, are mostly male and interested in start-ups and entrepreneurship. They do however work different hours, and have different ways of motivating their staff. While the PVCs focus a lot on money and the “fun factor” of working in this field the GVCs focus lies on the benefits to society, although they do enjoy their work. It is clear that in the PVCs one is expected to work long hours and as a reward earns high salaries and has an additional bonus of taking part of the reward if the found is successful. The GVCs on the other hand offer a higher level of work life balance. The only PVC where the investment managers are not part owner of the fund is SEB Venture Capital. At this company, the employees get regular salaries, and sometimes earn bonuses that make them similar to the GVCs in terms salary scheme.

The goals of the two types of funds also clearly differ. The PVCs want to make as much money as possible, while the GVCs do not focus on the money. However, there are other goals for example spreading investments throughout Sweden or being a good investor that educates the market. The empirical findings considering the differences in goals and employee motivation are illustrated in figure 16 below.

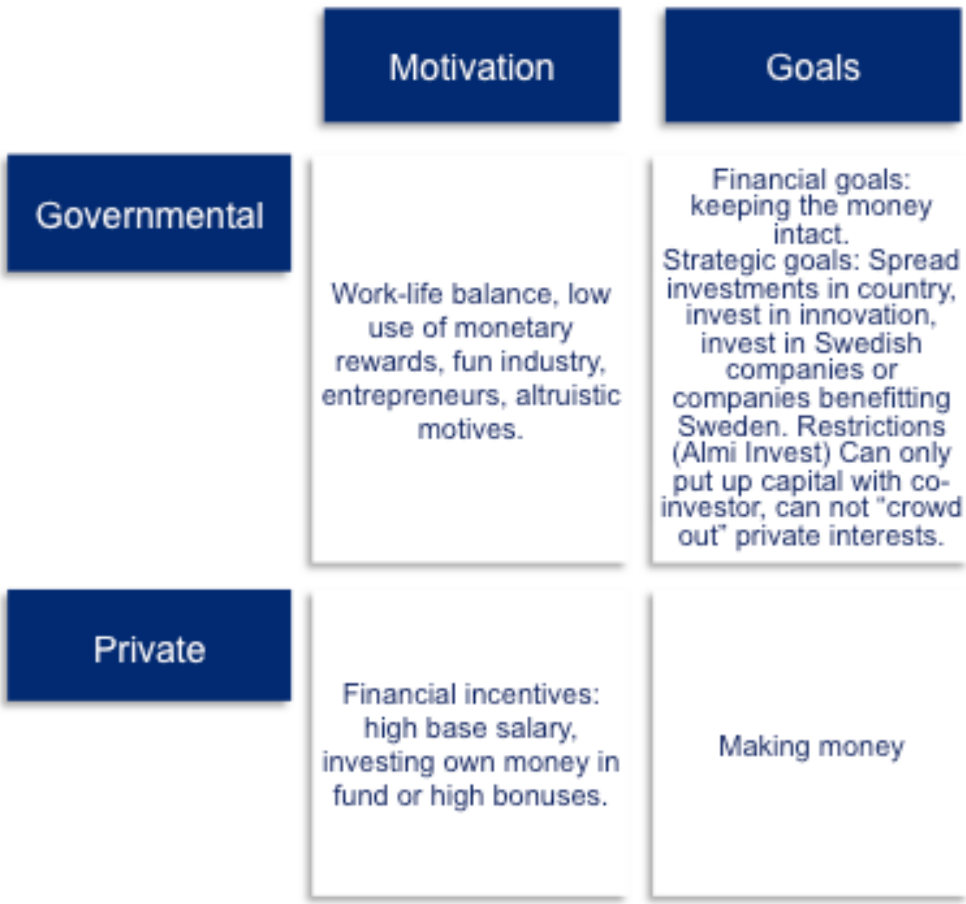

Figure 16: Summary of empirical findings related to goals and motivation

5 Analysis

After presenting the findings in the previous section, the following section is dedicated to the analysis of the findings in the light of the theory and outlines which steps of the investment decision process are affected. The analysis is structured according to our theoretical framework (figure 17) starting with the effects the form of venture capital firm has and proceeding downwards in the model, ending with the impact the previous steps have on the investment decision process of a venture capital firm.

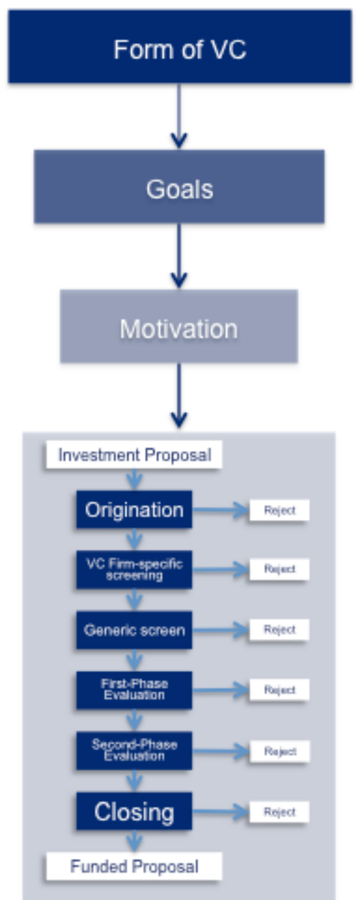

Figure 17: Theoretical Framework

5.1 Form of Venture Capital Firm

The goals and behaviour of the VC is shaped by several important factors, one being the organisational and legal structure of the company. In the literature section (2.3.1) the different types of VC are outlined and explained in detail. This literature review shows that the GVCs are normally captured ones, as they are under the influence of the government. When it comes to PVCs the majority is independent but in Sweden we can also find captured ones. Northzone, Creandum and EQT Ventures are examples of independent ones while SEB Venture Capital is a captured one. In the case of this sample the independent ones are all closed-end funds while SEB Venture Capital is an open-end fund.

The analysis conducted for this paper additionally revealed that there is not only a difference between a governmental and a private venture capital firm but also between an open-end and a closed-end fund. In the case of Sweden, this can be observed when comparing Almi Invest and Industrifonden. Almi Invest is a captured VC under the influence of the government when it comes to funding, goals and strategy. Industrifonden on the other hand can be classified as an independent VC, because they are only governed by their internal regulations. Industrifonden is designed to be an evergreen, open-end fund and their legal structure enables them to operate independently from the government. However, one of the drawbacks of being such an evergreen fund is that they will never receive additional monetary support. According to the conducted interviews, this makes the fund managers reluctant to take high risks concerning their investments, especially when it comes to the timing of the investment. They are more often than not, funding a company in later rounds than other VCs do. The upside of this setup is that they can keep their shares in their investments much longer than a normal closed-end fund.

The area where the form of VC manifests itself the most is when it comes to the goals of the fund. This difference in goals is outlined in the following section.

5.1.1 Goals

The analysis revealed that the form of the venture capital firm, namely being a private or a governmental one has a decisive effect on the goals the company is pursuing. While the private venture capital firms are driven by financial goals, the governmental ones have more strategic goals and an obligation to society. This is also in line with the findings of previously published research, which states that governmentally run VC funds not only have financial goals but also pursue strategic goals like employment creation or the promotion of competition and innovation within an economy (Brander, Egan, & Hellman, 2008).

5.1.1.1 Strategic Goals

The GVC Almi Invest has foremost strategic goals regarding the spreading of investments throughout the country, and their behaviour as an investor. The employees of Almi Invest believe that they are supposed to educate the market through good investor behaviour. Those strategic goals will certainly lead to differences in the investment decision process and ultimately the investments. For instance, Almi Invest responds to all of the incoming investment proposals, even the entrepreneurs that do not come into question for being granted an investment. Furthermore, Almi Invest is legally obliged to not crowd-out any private investors, possibly leading to a situation where they have to withdraw an investment proposal in case the money can be raised from private investors. They also have high ethical demands on their investments as well as regional restrictions allowing them to only invest in Sweden. All of these factors limit the scope the investments for Almi Invest. Industrifonden, also a GVC, does not have as harsh restrictions. The only guideline is that they are supposed to invest in innovative products and services that have a connection to Sweden. This enables them to invest more freely in businesses inside and outside of the country.

As elaborated, these strategic goals influence the behaviour of the governmental investors when it comes to the investment decision. The private ones on the other hand are mainly led by their financial goals rather than strategic considerations like educating the market.

5.1.1.2 Financial Goals

The private venture capital firms have clear financial goals – making three times the money invested is the norm among the questioned companies. In contrast, the GVCs have the financial goal of being a self-sufficient fund and keeping their capital base in tact. The financial goals are not only affected by the form of the VC firm, whether is governmental or private, but also by the structure of the fund itself i.e. if it is an open-end fund or a closed-end fund. The open-end funds, Industrifonden and SEB Venture Capital have a much more flexible investment horizon. Therefore, they are able to keep their shares longer and wait for the best time to exit, which on average is longer than the closed-end funds. Hence, open-end funds exert less pressure on the entrepreneur, since they have more time to reach their financial goals.

The fact of not having financial goals influences how the entrepreneurs view an investor. The analysis of the conducted interviews showed that for entrepreneurs, having a GVC as an investor gives a new venture more freedom to act as well as provides legitimacy and has a certain qualitative signal effect. Billhop for instance reports that Almi Invest as an investor is not interfering in their daily operations and lets them build the company the way they want. Furthermore, as a company offering financial services, Billhop indicated that having the Swedish government as one of their investors makes customers as well as other investors trust them. This is in line with evidence from previous research that shows that receiving governmental funding certifies new ventures and facilitates their access to qualified human as well as financial capital (Söderblom, Samulesson, Wiklund, & Sandberg, 2015). However, for the most part, the entrepreneurs are sceptic, considering governmental venture capital funds. In Niklas Agelvik's opinion, his investors should want to make money. It is important to have this goal as it influences the way he builds his company.

The financial goals are in some way restrictive however, because the PVCs and Industrifonden have to perform in order to survive while Almi Invest does not have the same pressure. Almi Invest do slightly more investments on a yearly basis. What could be a result of this "lack of monetary pressure" is a tendency to take more risk when investing. Indeed it is another goal that the GVC have, to spread the investments and capital more. If one does not have the same pressure to survive, one would act more risky because there is no threat in doing that, thereby enabling a spreading of investments. The government aims at balancing this tendency by imposing numerous restrictions on Almi Invest, in order not to see any of the adverse effects of risk taking behaviour. These requirements include that their board has to approve all the investments and the fact that they are only allowed to provide up to 50% of the total money raised in an investment round. This forces Almi Invest into a more generic VC position in the sense that they get more restricted in the sorts of investment they can do. Industrifonden lack the profit maximization goal of a private VC, however because of their evergreen structure they have strict financial restrictions due to the fact that they will never receive new capital. This forces Industrifonden to consider the financial implications of every investment. Hence, although having different (lower) financial goals, they behave similarly to a private VC fund.

As a result of analysing the goals of the venture capital firms, a visual representation of the different sorts of goals and how they relate to the fund structure has been created (figure 18). The different funds are placed in the matrix according to the information they provided during the interviews. Thereby, it becomes clear that the goal aspects are important in explaining the behaviour of the funds. For instance one can see that in some aspects Almi Invest is much more similar in its behaviour to the PVCs EQT Ventures, Northzone and Creandum, than to Industrifonden. However, as can be seen in the following section about human capital and motivation, the venture capital firms can also be grouped together in other ways depending on what the criteria are.

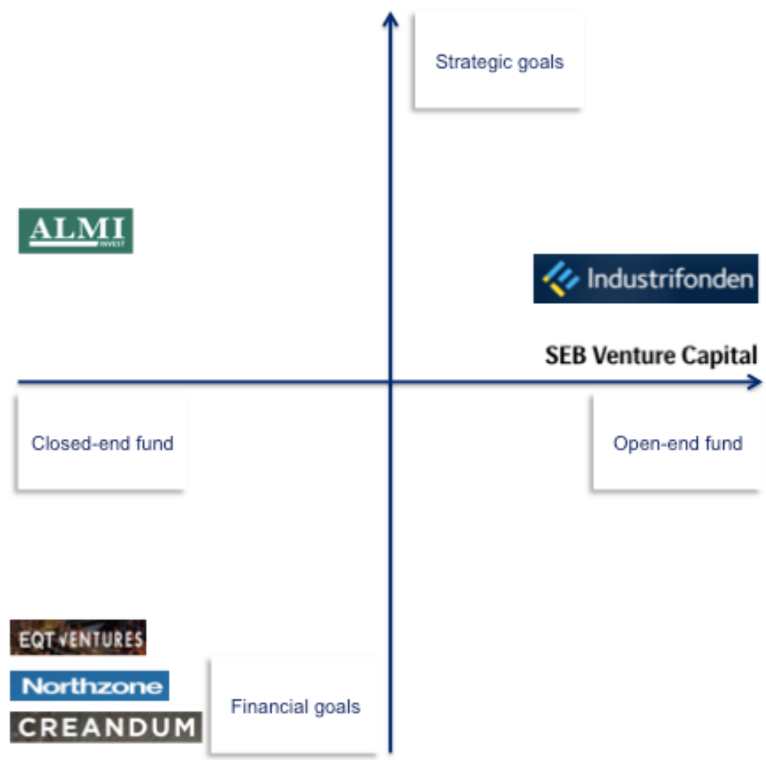

Figure 18: Matrix on timespan and goals

5.2 Human Capital

The nature of the goals (i.e. more financial or more strategic) a VC has, affects the motivation of their employees and therefore their human capital. According to the Resource Based View, the human capital is besides the monetary resources, the main resource a company has.

5.2.1 Intrinsic Motivation

Intrinsic motivation factors are hard to analyse. However, since intrinsic motivation is the motivation one gets from doing one's work itself, it can be assumed that it is the same for governmental and private VCs. Therefore, it is hard to argue that either the PVCs or the GVCs attract people with higher intrinsic motivation. It is also hard to say if a person has high intrinsic motivation or if it is extrinsic motivation that is making them work hard. Both of the groups have intrinsic motivation factors, such as meeting fun people, developing the economy and working on innovative ideas. Our conclusion is therefore that the GVC employees and the PVC employees both have intrinsic motivation at an equal level.

5.2.2 Extrinsic Motivation

Extrinsic motivation factors on the other hand, are more tangible. There is a clear difference in extrinsic motivation factors between GVCs and PVCs. The salary levels at the PVCs are higher and GVC employees are not required to buy into the fund, whereas PVC employees are. This means that PVC employees are essentially investing their own money, which – according to previous research – increases their vested interest in the company and their motivation to work harder (Pink, 2014). When asked how they motivate their staff, the high involvement one gets from investing one’s own money and the higher salaries they pay is also what the PVCs themselves mention.

Salary is a complicated motivation tool however. Money is a powerful motivator, but can also inhibit creativity and intrinsic motivation for ones work (Pink, 2014). The entrepreneurs suggest that the PVCs invest from fear of missing out, rather than from inspiration. Rather than thinking, “this is an interesting company” one might think “if we do not invest in this now, we might miss out on a great opportunity”. That type of behaviour can also be one explanation for the fact that the private VCs invest into the same companies. The extrinsic motivation then spurs the fear of missing out, giving rise to this grouping of investments. On the contrary, the analysis shows that the GVCs are not affected by this fear of missing out. They are uninhibited by this, as they are not allowed to invest in something if they risk crowding out other investors. They are also better at explaining their process, suggesting that they actually take the time to understand and go through their process more thoroughly and follow through on it. According to Hertzberg's model, base salary is a dissatisfier rather than a satisfier, suggesting that there is no reason to increase salaries if one wants to increase the employees' motivation (Pardee, 1990). From those factors one can conclude that, although it is good to have a highly motivated staff, it is not a good idea to try to extrinsically motivate them with money only. In fact, the employees' creativity might be stimulated if one does not try that.

Work-life balance is more important extrinsic motivator to GVC employees and when analysing the interviews it becomes clear that in a PVC people work longer hours. How hard the people work in the organisations, changes the amount of time spent on the companies in the portfolio and the research put into them prior to the investment. The work time spent is according to the venture capitalists themselves a very important factor in the quality of the process, which is also why they bring up motivation of the employees in the first place.

5.3 The Effects on the Investment Decision Process

In order to better understand how the differences in goals and human capital influence a VC's investment decision, Fried and Hisrich's (1994) investment decision process model is revisited in this section (figure 19). Looking at this framework enables us to pinpoint what steps differ between the various VC companies and how those affect the resulting decision to fund a new venture. Since the two screening steps as well as the two evaluation steps are not always perfectly distinguishable, they are merged to one screening and one evaluation step for this analysis. Furthermore, the conducted research has not shown any difference in the closing stage of the process between the interviewed companies. Therefore, the analysis of the process is structured into three different steps: *deal origination, screening* and *evaluation*.

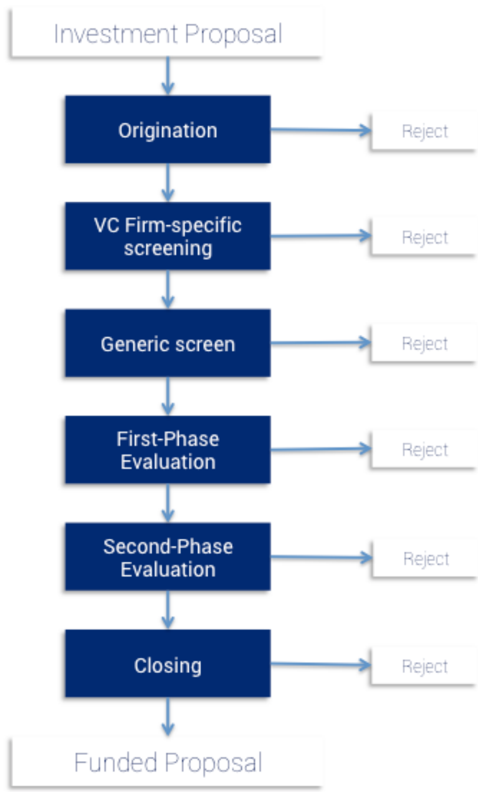

Figure 19: A VC's investment decision process (Fried & Hisrich, 1994)

5.3.1 Deal Origination

Although Fried and Hisrich's (1994) model is over 20 years old, the research done for this paper revealed that the VCs operating in Stockholm - no matter if they are funded privately, publicly or by a corporation - stick to the three ways of deal origination discovered in their study. Those are cold calls from entrepreneurs, referrals by a third party and the active search for potential investments by VC companies themselves.

5.3.1.1 Way of Finding new Companies

What is true for all of the in this study analysed VCs is that a great number of start-ups are applying for funding. While Almi Invest mentioned that they receive around 400 applications per year, EQT Ventures stated that they have gotten 500 requests for funding in a period of only two months and Northzone estimated to receive 800 investment proposals per year. According to Almi Invest cold calls from entrepreneurs are their only source of new deals, making them a rather passive player when it comes to deal origination. They state that they would prefer to be more active in finding new investment opportunities but due to their goal of educating the market they do not have the time to do so. This goal demands that they more closely analyse all the applications and give feedback and suggestions for improvement to every single one, taking up a lot of time.

The conducted research showed that for the private VCs on the other hand, referrals by third parties and the active search for companies to invest in are much more important channels. Staffan Helgesson from Creandum for example claimed that they have actively found and picket 50% of all the investments they have done so far. However, considering the fact that none of the other VCs has stated that the share of actively found companies is that high as well as the finding that all the interviewed entrepreneurs reported to have either approached their investor themselves or have been introduced to them by a third party suggests that Creandum is either an exception when it comes to deal origination or the number is an overestimation.

Overall, the analysis of the interviews shows that referrals by third parties and active search for deals are relatively more important sources for PVCs. However, it does not allow drawing any conclusions on the absolute importance of the different sources. Another important finding concerning the deal flow is that it is common practice for the venture capital firms in the Stockholm area to monitor a start-up over a long period of time (up to several years) before they decide to proceed and to actively pursue an investment opportunity.

The passive nature of Almi Invest's pursuit of investments might only be a perception however. The interviews revealed a lot of conflicting evidence reflecting how companies are found. All the private investors state that they find their investment opportunities themselves. However, the entrepreneurs indicate that they get their investments through longer periods of networking with the investor. The only concrete example of a venture capitalist "finding" a start-up to invest in comes from Creandum who discovered and approached Spotify. Analysing the interviews shows that within the venture capital industry it is considered more prestigious to personally find new investment opportunities. Johan Crona from Almi Invest for instance was almost apologetic for not actively searching for and finding investments. It seems that this narrative of "finding or discovering" the start-up companies, demonstrates an investor's abilities. Furthermore, the active discovery of a company by an investor proves their dedication to their work, and is evidence that they are motivated to find the best companies out there. As was explained on several occasions, it is time consuming to meet with entrepreneurs and search for investment opportunities. Therefore, only the most motivated investor engages in such behaviour. The aim of evoking this behaviour could explain the extensive employment of extrinsic motivation factors in PVCs.

5.3.1.2 Quality and Quantity of Companies in the Deal Flow

The regulatory directives they have to comply with foremost determine the sort of company Almi Invest invests in. Governmental investors in Sweden are by law not allowed to compete with the private ones in order to not crowd-out private money. Additionally, legislation demands Almi Invest to always have a private co-investor in order to make sure that their investments are done according to market terms. As a result they have access to different and fewer companies than the private investors.

Almi Invest stated that they often provide the remainder of the needed money, which a start-up is not able to raise through the private sector. Therefore, it could be argued that those start-ups are not competitive enough and might have worse prospects or are less popular among investors than the ones that are able to fully fund themselves on the private market. Indeed, today's market is well capitalized, which supports this argument. However, there is no evidence indicating that Almi Invest has lower qualitative expectations from their applicants.

Governmental ownership also affects the characteristics of the companies in the deal flow in another way. Since Almi Invest reinvests the Swedish tax money, it also has a geographical focus restricted to the Swedish market. They solely fund companies incorporated in Sweden resulting in solely Swedish companies asking for their money. The private VCs on the other hand are also open to invest in international firms. However, for the reason that a local proximity between investor and investee enables a better, more personal as well as more regular interaction between them, the interviewed private VCs prefer to invest in local companies.

Overall, the analysis of the research shows that the ownership structure of a VC i.e. governmental or private ownership, heavily influences the quantity and the nature of start-ups in the deal flow. On the other hand, some entrepreneurs also choose to take in a governmental investor on purpose in order to benefit from a signalling effect as well as an increased legitimacy (Söderblom et al., 2015; Andreescu, 2016). In this case, bringing in governmental investors might even increase the competitiveness of a new venture.

5.3.2 Screening

When asking the VCs how they proceed with the investment proposals two factors accounted for differences in the screening phase: the fact if the VC is governmentally funded or not and the sort of fund they manage i.e. open-end or closed-end.

The above-mentioned goal of Almi Invest and Industrifonden to not only fund companies but also educate the market leads to a more thorough screening of the companies that apply for an investment. This and the fact that they also give feedback to all the start-ups applying for funding implies that the screening stage is more time consuming for the Swedish governmental VCs in comparison to the analysed private VCs. Furthermore, the returns category (see figure 9 above) of the screening stage is different for open-end funds like the ones of SEB and Industrifonden compared to closed-end ones like Creandum, Almi Invest and Northzone. The reason for this is that closed-end funds have a fixed investment horizon while open-end funds are more flexible. Therefore, the exit opportunity is not that important for open-end funds as it is for closed-end ones. When it comes to the potential rate of return of a new venture, all the VC firms stated that the company has to have the potential to make them ten times the money they invest as their criterion for an investment. The screening stage is also the one mostly affected by the different employment of extrinsic motivators. Since the employees in private VC like Creandum or Northzone fully participate in the performance of the portfolio companies they have a strong personal interest in the investments they conduct. The analysis shows that the employees of the PVCs more thoroughly examine the start-ups that they are to invest in, no matter where in the world their offices are. This results in a lot of travelling, long days and makes it hard to maintain a good work-life balance.

However, there are also possible adverse effects of extrinsic motivators on the screening stage. For instance the FOMO behaviour, discussed in the theory section on motivation, can be seen at this stage. Start-ups that a VC would have not invested in, or that might not live up to all the screening criteria are “let through” at this stage because other investors are investing in them. This is a possible explanation for the fact that various VCs often invest in the same start-ups instead of creatively finding unique companies to invest in. Unfortunately, the GVCs are not allowed to reach their full potential to circumvent this phenomenon. The restriction on Almi

Invest to only invest with a co-investor effectively stops them from granting investments to companies that no other investor considers.

The research revealed that the other dimensions of the screening stage i.e. the size of the investment, the technology and market sector of the venture and the stage of financing depend more on the strategy of the respective VC company rather than on the fact if it is a private or a governmental institution or an open-end or closed-end fund.

5.3.3 Evaluation

The research showed that governmental and private VC firms use the same evaluation activities, which are also in line with what the existing theory (Fried & Hisrich, 1994) in this field states i.e. meet the management team, contact existing investors, contact potential customers, investigate the market value of the company etc. The main task in this stage is for all the VCs to align their strategy with the one of the entrepreneurs as well as with potential co-investors and existing investors.

5.3.4 Results from Process Analysis

The analysis of the process revealed that the origination stage is the longest one if one takes into account that venture capitalists often monitor a start-up over several years. Furthermore, the goals of a VC fund impact the origination stage. GVCs have the goal of educating the market, making them unable to actively search for investment opportunities. In addition to goals, motivation also impacts the origination stage. The extensive use of extrinsic motivators is a result of the aspiration to actively search for investment opportunities.

The screening stage is affected by the differences in goals, in a very obvious way. The screening is where the VC companies decide weather or not the venture lives up to their investment criteria. Therefore, the difference in financial and strategic goals separates the VC companies at this stage, as well as the open-end or closed-end nature of the funds. The extrinsic motivation factors also greatly influence the behaviour at this stage. It is clear that high use of monetary incentives provides hard working employees, however it also inhibits creative thinking in this stage. In the evaluation stage we can find no significant differences between the different kinds of VC firms. The further an investment proposal proceeds in the investment decision process, the more similar the activities of the different VC become and the less effect other factors like different goals or motivational schemes have.

6 Conclusion

What impact do the differences in the motivation of employees and goals between governmental and private VC companies have on their investment decision process? This is what the thesis seeks to answer in order to fill the identified gap in the existing literature. By analysing the major Swedish private and governmental venture capital investment companies, we aspired to find the differences in goals, and motivation of the employees. The results show that differences in goals and motivation schemes impact the investment decision process, in predictable and unpredictable ways.

By understanding the impact that these factors have on the investment decision process policy makers can further improve the governmental institutions and thereby use the tax money in a more efficient way. The findings can also help private institutions to further their understanding of their organisations.

6.1 Summary of main Findings

In the following section the main findings of this thesis are highlighted. Additionally, practical implications that these findings have for the development of the venture capital industry are derived.

6.1.1 Goals Matter

Goals matter but the question is how they influence the decision making process. Our study, similarly to what previous research states (Brander, Egan, & Hellman, 2008), proves that the goals differ between governmental and private venture capital firms. While the private venture capital firms pursue clearly stated financial goals, a number of non-financial aspects like promoting innovation or competition as well as employment creation are important for governmental venture capital companies. This difference in goals impacts the decision making process. Governmental venture capital firms are less likely to actively search for investments in the origination stage, as they believe that they have a greater responsibility to the cold call applicants for funding. Additionally, the private venture capital funds can invest in companies from all over the world as they have no geographical restrictions like the GVC.

Furthermore, our research suggests that some of the goals of the GVC are contradictory and can therefore inhibit their behaviour. Instead of spreading the investments as liberally as possible, numerous legal restrictions in the screening stage on the character of the investments force the GVCs to act more cautiously. This makes the GVCs behave more in line with a PVC. By acting more like a PVC the GVC is unable to reach some of the greater goals, for instance, spreading their investments.

The practical implication drawn from these findings is that financial and strategic goals are two extremes on a continuum. For a venture capital firm it is important to decide on what they are aiming for. When organising a governmental run venture capital fund it is therefore relevant for policy makers to review the impact that the goals that they decide on have on the process and in the end on the performance of the fund. For instance, if they have the higher goal of spreading investments it is not conducive to restrict the fund by not allowing it to make investments on its own. For the private investor it is important to take the time span of the investments into consideration. Having an open-end fund provides more flexibility thereby enabling the company to sell the shares at the best time and increase the probability to reach its financial goals.

6.1.2 Ambiguous Effects of Extrinsic Motivation

Considering the motivation of employees, the findings are that the intrinsic motivation is similar, no matter if one is working in a private or a governmental VC. However, extrinsic motivators, especially monetary ones, are applied to a much larger extent in the private venture capital firms. The reason for this is mainly their focus on financial aspects. Besides the purely financial goals, higher salaries, bonuses based on the fund's performance and the fact that they invest their own money in the fund, incentivize the employees. However, as research in the field of motivation states, extrinsic motivation not only has positive effects since especially monetary incentives might crowd-out an employee's intrinsic motivation as well as inhibit creativity thereby making it harder to preform well (Deci, Koestner & Ryan, 1999; Pink, 2014). One factor pointing to those negative aspects is the FOMO factor that leads the various venture capital companies to invest in the same start-ups. The positive effects of extrinsic motivation can be seen in the origination and screening stage of the investment decision process. The PVC employees work long hours and travel extensively to find and evaluate new business ideas.

Tying together the motivation with the investment decision process, the employees' extrinsic motivation influences the deal origination stage in how the investors find the investment opportunities i.e. either through actively searching for them or through only considering incoming applications for funding from entrepreneurs. It additionally affects the screening stage in several ways. For instance how much time and effort the employees put into the analysis of a new venture.

The implication of this is that it is not guaranteed that the implementation of monetary incentives leads to higher performing employees and a better performance of the VC company as a whole. Therefore, VC companies are recommended to apply other extrinsic incentives like work-life balance as well. When developing an incentive scheme it is therefore important to consider the positive and negative effects of each form of motivation. It is clear from our research that the private VC industry only considers the positive effects of high monetary incentives, however as previous research has shown there are not only positive effects. It is therefore recommended to organisations to carefully monitor and measure the effects of their incentive schemes.

6.1.3 The first Step in the Process

When examining the process, the results of the analysis show that Fried and Hisrich's (1994) investment decision process model used for this thesis does not adequately depict the process that the private as well as governmental investors go through. Therefore, we propose to add a first step, which depicts the long courting and networking period that both investors and entrepreneurs suggest exists before an investment opportunity enters the deal flow. This period can sometimes last for years and is described by the interviewees as an important part of the investment decision process.

6.2 Limitations of this Study

One limitation of this study is that motivation is an individual concern. It is hard to draw universally valid conclusions on how to motivate employees. Therefore, the more general conclusions drawn cannot be expected to apply to every single individual and organisation in the industry, which is why it is not possible to suggest a holistic incentive scheme. Another limitation is the subjective perspective of the interviewed people the results are based on. Due to time limitations, it was not possible for this study to observe the people in their daily work and get an objective view on the investment decision process they apply. Instead we have to rely on subjective statements on how they perceive their process to take place.

6.3 Suggestions for future Research

In order to diminish the limitation of the subjective nature of this study, future research is suggested to conduct a more in depth case study where the employees' behaviour throughout the investment decision process is observed. Thereby, the differences in their extrinsic motivation as well as its effect on the investment decision process at the different funds can be studied in a more objective way. It would also be interesting to take the industry narrative that we suggest exists in the VC industry as a starting point for future research and investigate how it affects the investors' behaviour. This is a very interesting phenomenon and is likely a strong influential force in the industry. This thesis solely concentrates on the investigation of the investment decision process without taking into consideration how this affects the performance of the different VCs. Upcoming research could shed more light into the actual differences in investment outcome between the governmental investments and the private ones. There already exists evidence that there is a difference in outcome, however, no publications deal with where this difference stems from.

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Appendix

Appendix I: Questionnaire for Entrepreneurs

Name of interviewee:

Company:

Founded:

Offices:

Employees:

Goals:

Investors:

1. Introduction of ourselves and the thesis topic
2. The interviewee introducing the company
    a. In what situation is the company is in right now?
    b. How many investment rounds have you already had?
    c. Who are your investors?
3. How did you decide on your investors?
    a. Did you approach your investors or did they approach you?
    b. Were you able to choose your investors or did you have to take what you got?
    c. What were the main reasons for choosing the ones you did? Why didn't you choose the others?

d. Why did you choose a governmental VC? Why did you choose a private VC?
e. According to your opinion, what is the difference between governmental and private ones VCs?
f. In case you have more than one investor: Why did you choose different investors and did not stick to one?

4. Describe the process that leads to an investment
    a. What happens from the introduction to an investor until you receive the term sheet?
    b. What were the criteria according to which you got assessed and chosen in every stage?
    c. Do you perceive the process that leads to an investment to be a standardized one? Is the process different for different VCs?
    d. Does it make a difference which other investors you already have on board? Is there a signal effect (positive/negative)?
5. Your current relationship with the investors?
    a. What is it like? Do your investors interfere in your daily operations?
    b. Do you talk to your investors on a regular basis?
    c. What is your report structure like?

Appendix II: Questionnaire for Investors

<u>Name of interviewee:</u>

<u>Company:</u>

<u>Founded:</u>

<u>Offices:</u>

Employees:

Goals:

Current portfolio companies (number and examples):

1. Introduction of ourselves and the thesis topic
2. The interviewee introducing the company
    a. What is the organizational structure of your company?
    b. What are the financial goals of your investments? Do you have other goals as well?
    c. What incentive schemes do you have in your company?
    d. What is your investment philosophy? What is your mission/vision statement?
    e. Do you have a preferred investment horizon? Is it a fixed or flexible time frame?
3. Describe the process that leads to an investment
    a. Do you search for companies to invest in or do they apply for funding?
    b. What happens from meeting the entrepreneur to issuing the term sheet? What are the steps you run through?
    c. What are the criteria according to which the companies get approved or rejected in every stage?
    d. Is there a standardized process that leads to an investment or is the process different for every start-up company?
    e. How are the decisions made in each step (e.g. democratic, top-down)?
4. Who are your competitors?
    a. What are your feelings towards your competitors?

b. What about governmentally/privately funded VC firms? Do you view them differently?

c. Do you prefer to be an early investor or rather later on?

d. Does it make a difference for you, which other investors (private/governmental VCs) are already on board? Is there a signal effect (positive/negative)?

5. How do you assess the performance of your company?

a. Do you consider your company to be successful? Are you meeting your goals?

b. What is your ROI?