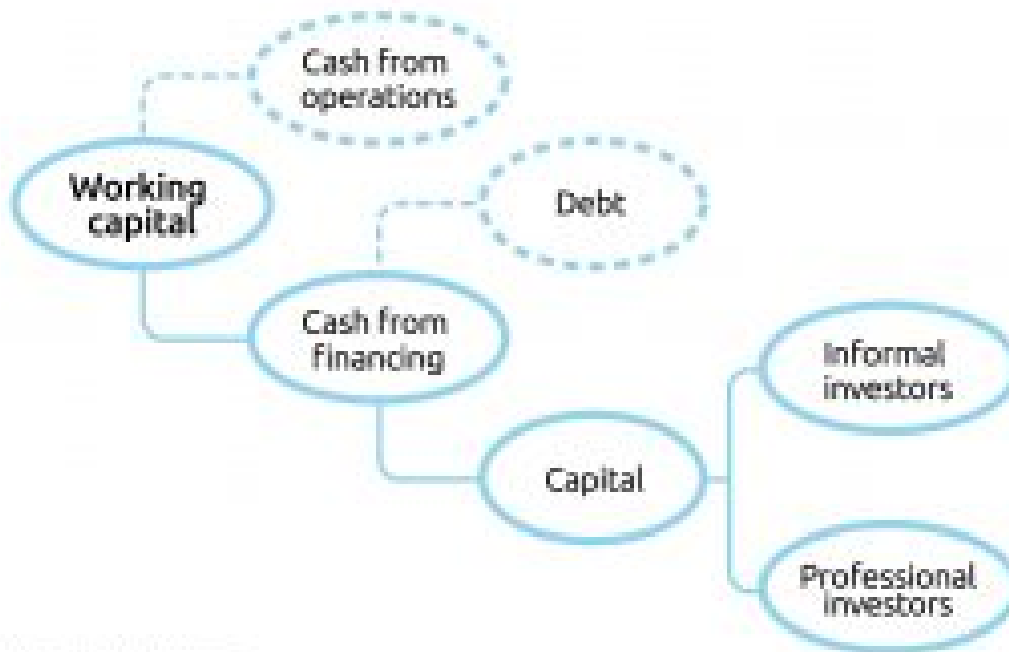


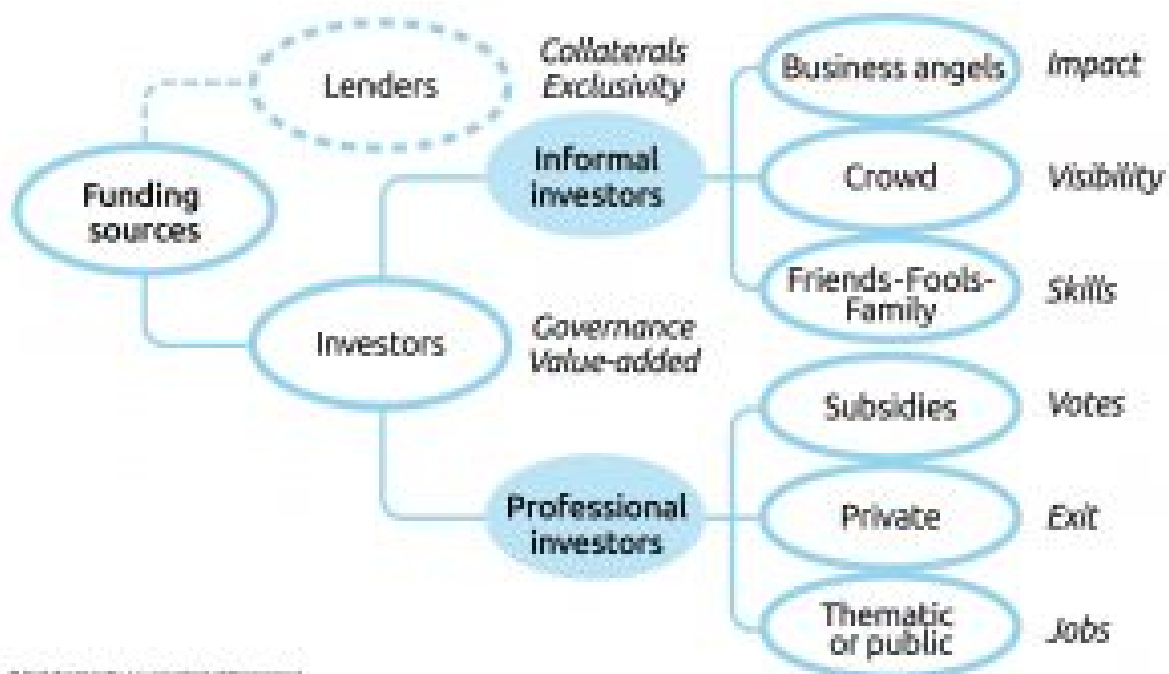
By Benoît Gailly, 17 January 2018

Smart money: funding innovation projects

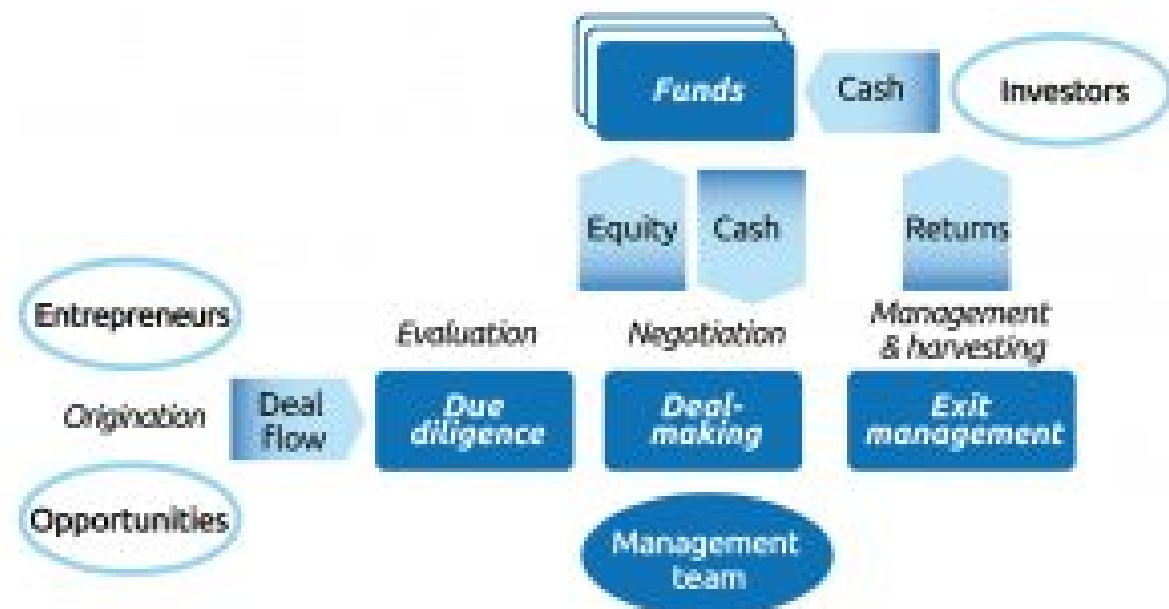


© 2018 Benoît Gailly, IPdigit (IPdigit.com)

The lack of track record, the ambiguity and the specificity of most innovation projects mean that innovation managers should consider alternative specialized **sources of financing**, such as informal and professional investors, to (co-)invest in the development of their opportunity.



Innovation managers and entrepreneurs looking for specialized outside (co-)investors must identify, target and engage effectively the right type of **financial stakeholders**, based on available offers, expectations and potential value-added.



Innovation managers and entrepreneurs can in some cases leverage the value-added and support of **venture capitalists** as (co-)investors, provided they master the business model of these

specialized investors, their selection criteria and their negotiation process.

Bibliography

Sources of financing: why cash is costly

Keywords: *adverse selection, agency costs, early-stage investors, information asymmetry, funding, smart money*

- (Book) Usselman, Steven W., Naomi R. Lamoreaux, and Kenneth Sokoloff. "[Financing Innovation in the United States, 1870 to the Present.](#)" (2007): 317.
- (Video) [Innovating the funding of innovation](#): Skyler Fernandes at TEDxConnecticutCollege
- (Article) Aghion, P., & Bolton, P. (1992). An incomplete contracts approach to financial contracting. *The Review of Economic Studies*, 59(3), 473-494.
- (Article) Anton, J. J., & Yao, D. A. (2002). The sale of ideas: Strategic disclosure, property rights, and contracting. *The Review of Economic Studies*, 69(3), 513-531.
- (Article) Bester H. (1985) "Screening vs. Rationing in Credit Markets with Imperfect Information", *The American Economic Review*; Vol. 75, No. 4 (Sep., 1985), pp. 850-855
- (Article) Berger, A. N., & Udell, G. F. (1998). The economics of small business finance: The roles of private equity and debt markets in the financial growth cycle. *Journal of Banking & Finance*, 22(6), 613-673.
- (Article) Carpenter, R. E., & Petersen, B. C. (2002). Capital market imperfections, high-tech investment, and new equity financing. *The Economic Journal*, 112(477), F54-F72.
- (Article) Cassar, G. (2004). The financing of business start-ups. *Journal of Business Venturing*, 19(2), 261-283.
- (Article) Coff, R. (2003). Bidding wars over R&D-intensive firms: Knowledge, opportunism, and the market for corporate control. *Academy of Management Journal*, 46(1), 74-85.
- (Article) De Clercq, D., & Dimov, D. (2008). Internal knowledge development and external knowledge access in venture capital investment performance. *Journal of Management Studies*, 45(3), 585-612.
- (Article) Freel, M. S. (2007). Are small innovators credit rationed?. *Small Business Economics*, 28(1), 23-35.
- (Article) Giudici, G., & Paleari, S. (2000). The provision of finance to innovation: a survey conducted among Italian technology-based small firms. *Small Business Economics*, 14(1), 37-53.
- (Article) Jensen, M.C., & Meckling, W.H. (1976). Theory of the firm: Managerial behavior, agency costs and ownership structure. *Journal of Financial Economics*, 3(4), 305-360.
- (Article) Kenney, M., & Zysman, J. (2019). Unicorns, Cheshire cats, and the new dilemmas of entrepreneurial finance. *Venture Capital*, 21(1), 35-50.
- (Article) Landier, A., & Thesmar, D. (2008). Financial contracting with optimistic entrepreneurs. *The Review of Financial Studies*, 22(1), 117-150.
- (Article) Lee, C., Lee, K., & Pennings, J. M. (2001). Internal capabilities, external networks, and performance: a study on technology-based ventures. *Strategic Management Journal*, 22(6-7), 615-640.
- (Article) Mason, C. M., & Harrison, R. T. (2002). Barriers to investment in the informal venture capital sector. *Entrepreneurship & Regional Development*, 14(3), 271-287.

- (Article) Mina, A., & Lahr, H. (2015). The pecking order of innovation finance. *Academy of Management Proceedings*, 1, 12786.
- (Article) Myers, Stewart C. and Majluf, Nicholas S., Corporate Financing and Investment Decisions when Firms Have Information that Investors Do Not Have (July 1984). NBER Working Paper Series, Vol. w1396, pp. -, 1984.
- (Article) Nanda, R., & Rhodes-Kropf, M. (2016). Financing risk and innovation. *Management Science*, 63(4), 901-918.
- (Article) O'Brien, J. P. (2003). The capital structure implications of pursuing a strategy of innovation. *Strategic Management Journal*, 24(5), 415-431.
- (Article) Stiglitz, J. E. (2000). The contributions of the economics of information to twentieth century economics. *The Quarterly Journal of Economics*, 115(4), 1441-1478.
- (Article) Stuart, P., Geoff Whittam, and Janette Wyper. "The pecking order hypothesis: does it apply to start-up firms?." *Journal of Small Business and Enterprise Development* 14.1 (2007): 8-21.

Navigating the innovation financing fauna: financial stakeholders

Keywords: *business angel, crowdfunding, FFF (friends, fools and family), investment funds, seed investing*

- (Book) Landström, Hans, and Colin Mason, eds. [Handbook of Research on Business Angels](#). Edward Elgar Publishing, 2016.
- (Book) Simon Parker (ed) [The Life Cycle of Entrepreneurial Ventures Kluwer](#); 2006
- (Video) [Choose the Right Investor for Your Startup](#) HBR Video
- (Article) Aghion, P., Van Reenen, J., & Zingales, L. (2013). Innovation and institutional ownership. *American Economic Review*, 103(1), 277-304.
- (Article) Ahlers, G. K., Cumming, D., Günther, C., & Schweizer, D. (2015). Signaling in equity crowdfunding. *Entrepreneurship Theory and Practice*, 39(4), 955-980.
- (Article) Belleflamme, P., Lambert, T., & Schwienbacher, A. (2014). Crowdfunding: Tapping the right crowd. *Journal of Business Venturing*, 29(5), 585-609.
- (Article) Berger, M., & Hottenrott, H. (2021). Start-up subsidies and the sources of venture capital. *Journal of Business Venturing Insights*, 16, e00272.
- (Article) Bruton, G., Khavul, S., Siegel, D., & Wright, M. (2015). New financial alternatives in seeding entrepreneurship: Microfinance, crowdfunding, and peer-to-peer innovations. *Entrepreneurship Theory and Practice*, 39(1), 9-26.
- (Article) Bugl, B. M., Balz, F. P., & Kanbach, D. K. (2022). Leveraging smart capital through corporate venture capital: A typology of value creation for new venture firms. *Journal of Business Venturing Insights*, 17, e00292.
- (Article) Burtch, G., Ghose, A., & Wattal, S. (2013). An empirical examination of the antecedents and consequences of contribution patterns in crowd-funded markets. *Information Systems Research*, 24(3), 499-519.
- (Article) Burtch, G., Ghose, A., & Wattal, S. (2015). The hidden cost of accommodating crowdfunder privacy preferences: A randomized field experiment. *Management Science*, 61(5), 949-962.
- (Article) Buterin, V., Hitzig, Z., & Weyl, E. G. (2019). A flexible design for funding public goods. *Management Science*, 65(11), 5171-5187.

- (Article) Carpentier, C., & Suret, J. M. (2015). Angel group members' decision process and rejection criteria: A longitudinal analysis. *Journal of Business Venturing*, 30(6), 808-821.
- (Article) Cumming, D. (2007). Government policy towards entrepreneurial finance: Innovation investment funds. *Journal of Business Venturing*, 22(2), 193-235.
- (Article) Croce, A., Tenca, F., & Ughetto, E. (2017). How business angel groups work: rejection criteria in investment evaluation. *International Small Business Journal*, 35(4), 405-426.
- (Article) Drover, W., Busenitz, L., Matusik, S., Townsend, D., Anglin, A., & Dushnitsky, G. (2017). A review and road map of entrepreneurial equity financing research: venture capital, corporate venture capital, angel investment, crowdfunding, and accelerators. *Journal of Management*, 43(6), 1820-1853.
- (Article) Grilli, L., & Murtinu, S. (2014). New technology-based firms in Europe: market penetration, public venture capital, and timing of investment. *Industrial and Corporate Change*, 24(5), 1109-1148.
- (Article) Harrison, R. (2013). Crowdfunding and the revitalisation of the early stage risk capital market: catalyst or chimera?; *Venture Capital*, 15(4), 283-287.
- (Article) Hsu, D. K., Haynie, J. M., Simmons, S. A., & McKelvie, A. (2014). What matters, matters differently: a conjoint analysis of the decision policies of angel and venture capital investors. *Venture Capital*, 16(1), 1-25.
- (Article) Kerr, W. R., Lerner, J., & Schoar, A. (2014). The consequences of entrepreneurial finance: Evidence from angel financings. *The Review of Financial Studies*, 27(1), 20-55.
- (Article) Kotha, R., & George, G. (2012). Friends, family, or fools: Entrepreneur experience and its implications for equity distribution and resource mobilization. *Journal of Business Venturing*, 27(5), 525-543.
- (Article) Maxwell, A.L., Jeffrey, S.A., & Lévesque, M. (2011). Business angel early stage decision making. *Journal of Business Venturing*, 26(2), 212-225.
- (Article) Mollick, E. (2014). The dynamics of crowdfunding: An exploratory study. *Journal of Business Venturing*, 29(1), 1-16.
- (Article) Oo, P. P., Allison, T. H., Sahaym, A., & Juasrikul, S. (2019). User entrepreneurs' multiple identities and crowdfunding performance: Effects through product innovativeness, perceived passion, and need similarity. *Journal of Business Venturing*, 34(5), 105895.
- (Article) Pahnke, E. C., Katila, R., & Eisenhardt, K. M. (2015). Who takes you to the dance? How partners' institutional logics influence innovation in young firms. *Administrative Science Quarterly*, 60(4), 596-633.
- (Article) Park, H. D., & Steensma, H. K. (2012). When does corporate venture capital add value for new ventures?. *Strategic Management Journal*, 33(1), 1-22.
- (Article) Paul, S., Whittam, G., & Wyper, J. (2007). Towards a model of the business angel investment process. *Venture Capital*, 9(2), 107-125.
- (Article) Politis, D. (2008). Business angels and value added: what do we know and where do we go?. *Venture Capital*, 10(2), 127-147.
- (Article) Shane, S., & Cable, D. (2002). Network ties, reputation, and the financing of new ventures. *Management Science*, 48(3), 364-381.
- (Article) Sonne, L. (2012). Innovative initiatives supporting inclusive innovation in India: Social business incubation and micro venture capital. *Technological Forecasting and Social Change*, 79(4), 638-647.
- (Article) Steier, L., & Greenwood, R. (2000). Entrepreneurship and the evolution of angel

financial networks. *Organization Studies*, 21(1), 163-192.

- (Article) Stevenson, R. M., Kuratko, D. F., & Eutsler, J. (2019). Unleashing main street entrepreneurship: Crowdfunding, venture capital, and the democratization of new venture investments. *Small Business Economics*, 52(2), 375-393.
- (Article) Van Osnabrugge, M. (2000). A comparison of business angel and venture capitalist investment procedures: an agency theory-based analysis. *Venture Capital: An International Journal of Entrepreneurial Finance*, 2(2), 91-109.
- (Article) Viotto da Cruz, J. (2018). Beyond financing: crowdfunding as an informational mechanism. *Journal of Business Venturing*, 33(3), 371-393
- (Article) Walthoff-Borm, X., Schwienbacher, A. & Vanacker, T. (2018). Equity crowdfunding: First resort or last resort?, *Journal of Business Venturing*, 33(4), 513-533,
- (Article) Warnick, B. J., Murnieks, C. Y., McMullen, J. S., & Brooks, W. T. (2018). Passion for entrepreneurship or passion for the product? A conjoint analysis of angel and VC decision-making. *Journal of Business Venturing*, 33(3), 315-332.

Professional innovation investors: Venture Capitalists

Keywords: bargaining, deal making, due diligence, syndication, venture capital

- (Book) Gompers, Paul Alan, and Joshua Lerner. [The venture capital cycle](#). MIT press, 2004.
- (Book) Landström, H. (Ed.) [Handbook of Research on Venture Capital](#) (2007),. Cheltenham, UK: Edward Elgar Publishing Ltd.,
- (Video) [Inside the mind of a venture capitalist](#) McKinsey Global Institute
- (Article) Amit, Raphael, James Brander, and Christoph Zott. "Why do venture capital firms exist? Theory and Canadian evidence." *Journal of Business Venturing* 13.6 (1998): 441-466.
- (Article) Bottazzi, L., Da Rin, M., & Hellmann, T. (2008). Who are the active investors?: Evidence from venture capital. *Journal of Financial Economics*, 89(3), 488-512.
- (Article) Brander, James A., Raphael Amit, and Werner Antweiler. "Venture-capital syndication: Improved venture selection vs. the value-added hypothesis." *Journal of Economics & Management Strategy* 11.3 (2002): 423-452.
- (Article) Bygrave, William D. "Syndicated investments by venture capital firms: A networking perspective." *Journal of Business Venturing* 2.2 (1987): 139-154.
- (Article) Bygrave, William D. "The structure of the investment networks of venture capital firms." *Journal of Business Venturing* 3.2 (1988): 137-157.
- (Article) Davila, A., Foster, G., & Gupta, M. (2003). Venture capital financing and the growth of startup firms. *Journal of Business Venturing*, 18(6), 689-708.
- (Article) De Clercq, D., Fried, V.H., Lehtonen, O., & Sapienza, H.J. (2006). An entrepreneur's guide to the venture capital galaxy. *The Academy of Management Perspectives*, 20(3), 90-112.
- (Article) Dimov, D., & De Clercq, D. (2006). Venture capital investment strategy and portfolio failure rate: A longitudinal study. *Entrepreneurship Theory and Practice*, 30(2), 207-223.
- (Article) Dimov, D., & Milanov, H. (2010). The interplay of need and opportunity in venture capital investment syndication. *Journal of Business Venturing*, 25(4), 331-348.
- (Article) Gompers, P., & Lerner, J. (2001). The venture capital revolution. *Journal of Economic Perspectives*, 15(2), 145-168.

- (Article) Gorman, Michael, and William A. Sahlman. "What do venture capitalists do?." *Journal of Business Venturing* 4.4 (1989): 231-248.
- (Article) Hellmann, T., & Puri, M. (2000). The interaction between product market and financing strategy: The role of venture capital. *The Review of Financial Studies*, 13(4), 959-984.
- (Article) Hellmann, T., & Puri, M. (2002). Venture capital and the professionalization of start-up firms: Empirical evidence. *The Journal of Finance*, 57(1), 169-197.
- (Article) Hsu, D. H. (2004). What do entrepreneurs pay for venture capital affiliation?. *The Journal of Finance*, 59(4), 1805-1844.
- (Article) Hsu, D. H. (2006). Venture capitalists and cooperative start-up commercialization strategy. *Management Science*, 52(2), 204-219.
- (Article) Jääskeläinen, M., Maula, M., & Murray, G. (2007). Profit distribution and compensation structures in publicly and privately funded hybrid venture capital funds. *Research Policy*, 36(7), 913-929.
- (Article) Kaplan, S. N., & Strömberg, P. (2003). Financial contracting theory meets the real world: An empirical analysis of venture capital contracts. *The Review of Economic Studies*, 70(2), 281-315.
- (Article) Kortum, S., & Lerner, J. (2000). Assessing the contribution of venture capital to innovation. *RAND Journal of Economics*, 674-692.
- (Article) Manigart, S., Lockett, A., Meuleman, M., Wright, M., Landström, H., Bruining, H., & Hommel, U. (2006). Venture capitalists' decision to syndicate. *Entrepreneurship Theory and Practice*, 30(2), 131-153.
- (Article) Sahlman, W. A. (1990). The structure and governance of venture-capital organizations. *Journal of Financial Economics*, 27(2), 473-521.
- (Article) Sapienza, Harry J. "When do venture capitalists add value?." *Journal of Business Venturing* 7.1 (1992): 9-27.
- (Article) Shepherd, D. A., Ettenson, R., & Crouch, A. (2000). New venture strategy and profitability: A venture capitalist's assessment. *Journal of Business Venturing*, 15(5-6), 449-467.
- (Article) Sorenson, Olav, and Toby E. Stuart. "Syndication networks and the spatial distribution of venture capital investments 1." *American Journal of Sociology* 106.6 (2001): 1546-1588.

(c) Prof. Benoit Gailly, Louvain School of Management