Fan Wang

FROM RELATIONAL CAPITAL TO VENTURE CAPITAL

FINANCING ENTREPRENEURIAL INTERNATIONAL NEW VENTURES
FAN WANG

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Financing entrepreneurial international new ventures.

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Abstract

The purpose of this study is to explore the role of relational capital in raising and utilizing venture capital by international new ventures (INVs). This study reviews literature on INVs, venture capital, and social capital theory and defines relational capital as the level of trust developed in the course of interactions between INVs and venture capital firms (VC firms) that leads to positive venture capital decisions and value creation.

This empirical study of relational capital formation and utilization is accomplished by the case study method. The study is based on interviews with five case INVs regarding entrepreneurs’ and venture capitalists (VCs)’ experiences with forming and utilizing relational capital for the purpose of new venture internationalization. This study approaches the relationship between INV and VC firm from the relational capital perspective, exploring how INVs can raise venture capital for internationalization as well as how they can use relational capital to improve outcomes of new venture internationalization after venture capital is allocated. The analysis identifies the factors that affect formation of relational capital between INVs and VC firms, the outcomes that result from relational capital formed in the pre-investment stage, and the impact on performance of INVs during post-investment collaboration.

This study develops a conceptual model proposing that the financing process for entrepreneurial INVs consists of forming and using relational capital to obtain venture capital investment. The particular characteristics of the INVs and VC firms, as well as behavior-related factors, have been found to be important to forming relational capital between INVs and VC firms. The relational capital formation process creates an atmosphere in which entrepreneurs and VCs provide both tangible and intangible resources to support INV internationalization. This study adds the relational capital viewpoint to the literature pertaining to venture capital and INVs by analyzing the role of relational capital in financing entrepreneurial INVs. Regarding managerial implications, the study shows how entrepreneurs can influence the venture capital investment process, where VC firms should pay attention to while working with INVs, and how policy makers could contribute by providing a positive environment for INV and VC firm collaboration.

Keywords: entrepreneurship, international new ventures, relational capital, venture capital
Tässä tutkimuksessa tarkastellaan kansainvälisiin uusiin yrityksiin tehtyjä pääomasijoitusprosesseja suhdepääoman muotoutumisen ja hyödyntämisen näkökulmasta. Tutkimuksessa aihetta lähestytään sekä yritysten että pääomasijoittajien kannalta ja työn teoreettinen viitekehys rakennetaan kansainvälisten uusien yritysten, pääomasijoitusprosessin, ja sosiaalisen pääoman tutkimusjulkaisujen kautta. Työssä suhdepääoma määritellään luottamukseksi, joka kehittyy vuoro-vaikutuksen kautta yrityksen ja pääomasijoittajan välille ja johtaa positiiviseen pääomasijoitus-päätökseen ja arvonluontiin.

Työn empiirisessä osassa suhdepääoman muotoutumista ja hyödyntämistä tutkitaan tapaus-tutkimusmenetelmällä. Tutkimuksen aineisto on kerätty haastattelumallalla viiden kansainvälisten nuoren yrityksen yrittäjien ja pääomasijoittajien tapauksista yrittäjien ja pääomasijoittajien kokemuksista yrityksen kansainvälistä kasvua rahoittamiseksi. Työssä analysoidaan suhdepääomaa muodostumisprosessin ja sen vaikutuksia yrityksen kansainvälistymiseen. Analyysiä avustaa myös aineistomateriaali, joka on kerätty haastattelumallalla yritysryösteltä yrittäjien ja pääomasijoittajien kokemuksista yrityksen kansainvälistymiseen ja suhdepääomaa.

Asiakirjan tavoitteena on tarkastaa suhdepääoman muotoutumisen ja hyödyntämisen vaikutukset yrityksen kansainvälistymiseen. Tutkimuksen avaruudessa on osoitettu, että suhdepääoma muodostaa ilmapiirin, jossa yrityksen ja pääomasijoittajan välinen suhde pysyy ja kehittyy. Työssä osoitetaan, että suhdepääoma muodostaa suhdepääomaa, joka myös vaikuttaa pääomasijoitukseen ja yrityksen menestykseen. Työssä on käytetty erityisesti suhdepääoman merkitystä yrityksen kansainvälistymiseen ja suhdepääomaa käsiteltyä erityisesti yrityksen kansainvälistymisen tukeena ja vaikutuksena yrityksen menestykseen.
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Fan Wang
Abbreviations

etc. et cetera

e.g., exempli gratia

CEO Chief Executive Officer
CFO Chief Financial Officer
EU European Union
ICT Internet Communication Technology
INV International New Venture
IPO Initial Public Offering
IPR Intellectual Property
M&A Merger and Acquisition
ROI Return on Investment
R&D Research and Development
U.S. United States
VC Venture Capital
VCs Venture Capitalists
Contents

Abstract ................................. 1
Tiivistelmä .................................. 7
Acknowledgements .................. 11
Abbreviations ......................... 13
Contents ................................. 17

1 Introduction ................................
1.1 Theoretical setting of the study................................. 18
1.2 Objectives and research questions .............................. 24
1.3 Key concepts ......................................................... 26
1.4 Methodological approach and empirical setting of the study.............. 27
1.5 Planned contribution of the study ............................... 30
1.6 Structure of the study .............................................. 32

2 INVs, venture capital, and internationalization .......................... 37
2.1 International new ventures ....................................... 37
  2.1.1 Entrepreneurs in international new ventures .................. 40
  2.1.2 Network relationships of international new ventures .......... 41
2.2 Venture capital investment and process .......................... 43
  2.2.1 Pre-investment phase ............................................ 44
  2.2.2 Post-investment phase ......................................... 46
2.3 Review of venture capital and portfolio ventures’
  internationalization ................................................. 50

3 Theoretical framework of relational capital in the venture capital
  process for new venture internationalization .......................... 55
3.1 Points of view on entrepreneur and venture capitalist dyad relationship ................................................. 55
3.2 Defining relational capital .......................................... 57
3.3 Formation of relational capital in pursuit of venture capital for
  internationalization .................................................... 60
  3.3.1 In the origination phase ........................................ 61
  3.3.2 In the screening phase ......................................... 62
  3.3.3 In the evaluation phase ........................................ 62
  3.3.4 In the deal structuring phase ................................ 66
3.4 The utilization of relational capital for internationalization in the
  post-investment phase ................................................. 67
  3.4.1 Monitoring ...................................................... 68

13
3.4.2 Value-added services ................................................................. 70
3.5 Theoretical model: *a priori* model .............................................. 74

4 Research design 81
4.1 Research philosophy ................................................................. 81
4.2 Case study design ...................................................................... 82
4.3 Data collection ........................................................................... 85
4.4 Data analysis ............................................................................ 93

5 Empirical analysis of relational capital formation and utilization 99
5.1 The backgrounds of the cases .................................................... 99
5.2 Capturing the formation and utilization of relational capital in individual cases ................................................................. 102
5.2.1 Individual INVs’ case studies described by entrepreneurs ...... 102
5.2.2 VCs’ collective understanding ............................................... 114
5.2.3 Comparisons between the two groups .................................. 118
5.3 Capturing the formation of relational capital ......................... 120
5.3.1 New venture internationalization ......................................... 120
5.3.2 Appropriate referral .............................................................. 126
5.3.3 Interaction between INV and VC firm ................................. 133
5.3.4 Controlling for liabilities and costs ..................................... 138
5.3.5 Valuation of the INV .......................................................... 144
5.4 Exploring the utilization of relational capital ....................... 150
5.4.1 Alignment between INV and VC firm ................................. 151
5.4.2 Value appropriation from VC firm’s network and resources .............................................................................. 155
5.5 Issues emerging from the data ................................................. 159
5.5.1 External environment ............................................................ 159
5.5.2 Human factors ...................................................................... 162
5.5.3 Luck or opportunity ............................................................... 165
5.6 Cross-case analysis ................................................................. 166
5.6.1 The role of relational capital in raising foreign venture capital ................................................................. 166
5.6.2 Entrepreneurial power in negotiations with VCs .................. 167
5.6.3 The perceived relational atmosphere .................................. 169
5.7 Empirical model ........................................................................ 172

6 Discussion 179
6.1 Overview and discussion of findings ........................................ 179
6.2 Discussion related to the research questions ............................ 182
6.3 Conceptual model: *a posteriori* model...................................................... 186

7 Conclusions 193
7.1 Conclusions of the study................................................................. 193
7.2 Theoretical contribution................................................................. 198
7.3 Practical implications................................................................. 202
7.4 Evaluation of the study ................................................................. 205
7.5 Limitations of the study ................................................................. 207
7.6 Avenues for further study................................................................. 208
7.7 Research summary ......................................................................... 210

Reference 213
Appendices 231
1 Introduction

“The relationship between an entrepreneur and a venture capital investor is similar to a marriage. There are ups and downs, and over time they face situations that can leave them richer or poorer. Through it all, there needs to be a fundamental trust between both sides.” – Forbes

This study starts with contemplating these foundational questions: how do small high-tech startups manage to raise funding for their internationalization, why do they choose venture capital as the means of funding, and how can they raise and work with venture capital? Academic studies tell various stories of successful startups that have been backed by venture capital in the United States (U.S.). However, few studies have focused on Finland, which is famous for innovation and high technologies, particularly in the information and communication technology (ICT) industry. Due to limited domestic market demand and the nature of their products, Finnish startups internationalize right after inception.

The government of Finland provides grants and loans for small business development and offers special startup grants for high-technology and potentially high-growth firms. Finnish entrepreneurs usually start their search for funding by applying for government funding from multiple providers, such as the Finnish Innovation Fund known as Sitra, and Tekes. Meanwhile, entrepreneurs actively search for other alternative financial instruments such as angel investors and venture capital before they have earned the credibility necessary to be approved for bank loans. Statistical data shows that the amount of venture capital available in Finland is rather small compared to the U.S., and the venture capital market is extremely competitive for the thousands of startups vying for the limited funds. Indeed, many Finnish startups travel to the Silicon Valley in the U.S. to seek venture capital.

The key related questions that tend to persist are “how can these startups pitch new venture internationalization to venture capital investors?” “Why are some entrepreneurs successful in raising venture capital, while others are not?” “How can entrepreneurs maintain relationships with domestic and foreign VC firms?” The standard answers are that “relationships matter” or “it’s all about your network.” Therefore, this study investigates the relationship between international new ventures (INVs) and venture capital (VC) firms and explores how relational capital affects the financing outcomes for entrepreneurial INVs.
1.1 Theoretical setting of the study

The rapidly changing global business environment and advanced communication technologies have created unprecedented opportunities for small, young companies to extend their sales across international borders. Those companies that have engaged in international business from early in their inception are commonly referred to as “international new ventures” (McDougall & Oviatt 1996). These startups boldly venture abroad, all the while searching for financial capital and strategic management advice to develop an international market and cope with the challenges faced in internationalization. Despite limited resources and capabilities, small technology firms increase their likelihood of survival by engaging in sales internationalization (Lee et al. 2012). These firms also use the opportunity of international expansion to achieve growth (Cumming et al. 2009, Soriano & Dobon 2009).

Five potential liabilities are common to INVs engaging in internationalization. These liabilities imply specific challenges for venture capitalists (VCs) when selecting and supporting INVs. The first two liabilities, newness and inexperience, hinder new ventures in obtaining valuable resources in existing networks (Nagy et al. 2014). The third liability relates to the small size of INVs, which challenges the survival of the new ventures’ internationalization processes (Zahra et al. 2005). The fourth liability relates to the natural barriers that arise from attempting to enter a foreign market and access potential suppliers and customers in an unfamiliar country (Zaheer & Mosakowski 1998). Schweizer et al. (2010) consider internationalization is an incidental outcome, or a “happy accident” of the usual entrepreneurial process. However, INVs usually lack business partners and knowledge in established foreign networks, which creates another barrier to market entry. As such, the fifth liability faced by new ventures is so-called “outsidership” (Johanson & Vahlne 2009).


VC firms are a financial intermediary specializing in raising funding to invest in unquoted, early-stage, startup companies with a high potential for growth, where the primary reward is an equity share in the company and an eventual capital gain, supplemented by dividends. A group of professional investors operates as the go-
between for the ultimate investor and entrepreneur. Venture capital investors provide not only financial support, but also often valuable strategic advice for creating successful companies such as Google, Microsoft, Apple, and Facebook. Venture capital has backed thousands of well-known entrepreneurial firms that make significant contribution to economic growth in developed countries, most notably in the U.S. (Manigart et al. 2000, Robbie & Mike 1998).

Besides venture successes, VC investment also involves significant risks that led to the development of a rigid venture investment process involving the evaluation, monitoring, and control of new ventures that lack business track records. With its rich and fascinating history, the study of the VC industry has been an important research topic related to the field of entrepreneurship for many decades (De Clercq & Manigart 2007, Kaplan & Strömberg 2003b, Timmons & Bygrave 1986, Tyebjee & Bruno 1984).

In response to continued entrepreneurial internationalization, studying the impact of VC on new venture internationalization has been of particular interest in recent years (George et al. 2005, LiPuma 2006, Lockett et al. 2008, Lutz & George 2012, Smolarski & Kut 2011). Carpenter et al. (2003) in their study have shown that VCs tend to see new venture internationalization as too fraught with risk to pursue, to the point that they favor domestic strategy over internationalization unless they are able to place an internationally experienced director on the board of the new venture, and similarly experienced people in management positions.

As the VC industry itself has recently started to enter international markets and often lacks foreign investment experience and knowledge, the internationalization of their portfolio new ventures complicates the situation due to the limited abilities of the VCs to monitor distant operations (De Prijcker et al. 2012, LiPuma 2012). Nevertheless, George et al. (2005) in their research have demonstrated that external ownership, including both corporate VC investors and VCs, encourages VC-backed INVs to become engaged in foreign business operations.

From the international performance perspective, VC involvement has increased the scale, scope and speed of internationalization (George 2005, LiPuma 2006, Lockett et al. 2008, Lutz & George 2012, Smolarski & Kut 2011, Zahra 2007). On the other hand, Lipuma (2006) has revealed that early internationalization decreases the valuation of firms in their initial public offerings, which can result in VCs’ reluctance to allow their portfolio companies to enter foreign markets. Moreover, Smolarski and Kut (2011) have shown that firms engaged in internationalization may benefit from VCs’ efficient monitoring and risk management.
However, too many restrictions also can cause negative effects on internationalization activities and performance, as INVs need greater operational flexibility to deal with the magnified uncertainties of international business operations. Venture capital might not be favored for internationalization if VCs lack the knowledge and resources to support internationalization activities (George et al. 2005). The debates on this subject in prior literature center around venture resources, control issues, and valuation of exit when considering whether VC firms should invest in early internationalization. The mixed performance results of VC-backed early internationalization make the phenomenon complex to understand.

VC involvement accelerates the INV internationalization process and increases the export intensity of the VCs’ portfolio of firms. This research result is supported by (Fernhaber & McDougall-Covin 2009, George et al. 2005, LiPuma 2006, Lockett et al. 2008, Lutz & George 2012, Smolarski & Kut 2011). Current research has made progress in understanding the relationship between VC involvement and new venture internationalization. Nevertheless, the relevant studies on this topic mainly focus on testing whether there is a relationship between VC investment and new venture internationalization, either positively or negatively. Research on value-added services and mechanisms through which VCs add value to internationalization of new technology ventures has not yet been conducted (Maula 2001).

Despite the insights offered by this rapidly growing research stream, relatively little is known about “the precise nature of venture capital resources in relation to international activities” (Lockett et al. 2008: 55). Given the importance of internationalization as a strategy for a new venture’s growth and survival (Mudambi & Zahra 2007), it is important to understand how and where venture capital affects early internationalization of new ventures (Zahra et al. 2007).

With the groundwork of the foregoing discussion, the crucial issue is not to test the existing relationship between VC investment and international performance. Rather, the important issue is to understand the instrument or mechanism by which VC firms are willing and able to add value to the internationalization process of new ventures and the interactive processes taking place between INVs and VC firms to appropriate value. This study is devoted to filling in this research gap and discussing relational capital as a mechanism to consider the dyad relationship between INVs and VC firms and to study the value creation that occurs when the two actors join forces.

This dissertation discusses the concept of “relational capital” and investigates the interaction that takes place between INVs and VC firms. Unlike other research
devoted to identifying social-relational capital as a mechanism for building resources around INVs (Lee et al. 2001), the main objective of this study is to capture how INVs develop their early internationalization processes at the same time as developing relational capital with their financial resource providers/VC firms.

Bygrave (1987, 1988) proposed that networks were important for U.S. VCs. The further exploration by Shane & Cable (2002) and Stuart et al. (1999) has supported this view with a large sample survey. The influence of networks on venture capital and its importance has received wide acknowledgment (e.g., Ahlstrom & Bruton 2006, Sorenson & Stuart 2008) in the field. However, relational capital rooted in social network theory has not yet been widely applied in venture capital research due to the dominance of agency and stewardship theories as approaches to viewing the entrepreneur/venture capitalist dyad relationship.

In the venture capital context, the agency theory is often applied to investigate the relationship between entrepreneurs and VCs. Agency problems (Jensen & Meckling 1976, Kaplan & Strömberg 2003b) including goal incongruence, information asymmetry, and moral hazards (De Clercq & Sapienza 2001, Eisenhardt 1989a) result from separate ownership of and control in companies. From the agency perspective, the entrepreneur is considered an agent who might act opportunistically upon the interests of the VC firm as principal. The agency theory has received criticism due to its neglect of the relational-social nature of the relationship and its inadequate explanation of why the goals of the entrepreneur and VC firm (Arthurs & Busenitz 2003) are not aligned even after the careful venture capital decision-making process and monitoring (Manigart et al. 2002, Sapienza & Gupta 1994).

Another dominant approach to studying the entrepreneur/venture capitalist dyad relationship is the procedural justice theory, which focuses on trust and fairness of treatment by VCs. The procedural justice theory takes the relational aspect of the dyad relationship into account and focuses on interpersonal relationship development (Sapienza & Korsgaard 1996, Sapienza et al. 2000). However, the procedural justice theory assumes the power of the venture capitalist is much stronger than the entrepreneur’s, relegating the entrepreneur to the position of a subordinate to the venture capitalist (Lehtonen 2006).

The stewardship behavior approach is organization-centered and argues that entrepreneurs with the need for self-esteem, self-actualization, growth, achievement, and affiliation seek to improve organizational performance by satisfying the VCs in the entrepreneur/venture capital context (Arthurs & Busenitz...
The application of stewardship theory emphasizes aligning the interests of the entrepreneurs with the VCs by sacrificing the needs of entrepreneurs.

Both the procedural justice theory and stewardship approaches have largely neglected the power of the entrepreneur. Additionally, the stewardship approach fails to explain power when the goals of the entrepreneur and venture capitalist are not aligned before venture capital decision-making. That is, the goal of the VC firm is to avoid bad investment, whereas the goal of the entrepreneurial firm is to successfully obtain venture capital (Arthurs & Busenitz 2003).

This study implements relational capital as a means of looking at the relationship between INVs and VC firms and provides a rich base for understanding the social-relational nature of dyad relationships (Bruton et al. 2005, Shane & Cable 2002). The concept of relational capital acknowledges that the power of the entrepreneur is equal to that of the VC firm and interprets the relationship with VCs from the entrepreneur’s perspective. In this study, the venture capital investment process is seen as a relational capital building and utilization process that adds value to both parties throughout the entire venture capital investment period.

General consensus holds that relational capital allows entrepreneurs to gain access to venture capital (Liao & Welsch 2005) in the pre-investment stage. However, the link to VCs through relational capital does not guarantee a positive funding decision for internationalization. The research studying the relationship formation efficiency that affects the success and duration of the raising of venture capital can be seen as supporting this line of reasoning (Hallen & Eisenhardt 2012). The question of whether (and, if so, how) relational capital between entrepreneurs and VCs supports raising of VC investment remains unexplored. Although (Alexy et al. 2011, De Clercq & Sapienza 2006, Hallen & Eisenhardt 2012) in their studies point out the importance of relational capital in a venture capitalist’s decision-making process, how exactly it affects the funding decisions for international new ventures still demands systematic research.

As a form of utilization of relational capital, VC-backed new ventures not only receive funding and strategic advice (Fried & Hisrich 1994, Hsu 2005), but also valuable network contacts and partnering opportunities (Sarkar et al. 2001) with recruiters, patent lawyers, investment bankers (Hochberg et al. 2007), key suppliers, and customers with whom VCs are connected. INVs usually lack the track record and internal resources necessary to commercialize their products in global markets (Baum & Silverman 2004, Baum et al. 2011, Freeman et al. 2006). McDougall (2004) argues that without owning all the necessary resources, new ventures rely
heavily on this network to access vital assets for early internationalization. Building the network capabilities of new ventures is important for internationalizing to third countries. How INVs can obtain added value, provide a wide range of opportunities for, and facilitate the VC-funded internationalization process using relational capital as a mechanism awaits further exploration.

This study focuses extensively on the formation and utilization of relational capital between VC firms and INVs. More specifically, this study attempts to provide a general understanding of the role of relational capital in raising venture capital for resource-constrained INVs and the role it plays in the early internationalization process. Through a systematic review of INVs, network, venture capital literature and relational capital, the role and importance of relational capital in venture capital process have been given my own theoretical understanding as shown in Figure 1.

Figure 1 depicts the steps involved in forming relational capital within the venture capital investment process. The time frame of the study extends from the point of approaching the VC firm to the point of exit, or immediately before. Any activities that occur before the stage of approaching venture capital will not be discussed in detail, nor will activities after exit be covered by this dissertation. This study focuses on events and activities between INVs and VC firms during the venture capital process and does not deal with the financial calculation of valuation, such as precedes an initial public offering (IPO). These events and activities between INVs and VC firms help create an understanding of relational capital for new venture internationalization, thus achieving the purposes of the research.

![Fig. 1. Scope of the research](image-url)
The venture capital investment decision is the critical point that divides the investment process into two distinct stages: the pre-investment stage (before the investment decision is made) and the post-investment stage (after the investment decision has been made). With deliberateness, this study considers the pre-investment process as the stage of building or forming relational capital, because the relationship between the INV and VC firm is still dynamic in the pre-investment stage.

In the pre-investment stage, the study aims to understand the importance of forming relational capital between the two parties and to clarify the role relational capital plays in raising venture capital. The study will take both entrepreneurs’ and VCs’ perspectives into consideration to generate a holistic picture that illustrates the unique value of relational capital for each party.

Utilization of relational capital occurs during the post-investment stage, as INVs and VC firms have at this point established a formal relationship and jointly make decisions about the activities and events to take place in the new venture internationalization process.

The focus will then shift to understanding how relational capital developed during the pre-investment stage and used during the post-investment stage can benefit the early internationalization process of new ventures. In sum, the scope of this research is to understand the process of VC firms and INVs forming and using relational capital throughout the entire investment process.

### 1.2 Objectives and research questions

There are two types of objectives to the study: the theoretical objective and the empirical objective. The theoretical objective of the research is to identify the factors that potentially influence whether and how INVs form relational capital by tracing each step of the pre-investment stage through the expected outcomes of relational capital utilization for new venture internationalization. In reaching this objective, the study will develop a theoretical model of relational capital formation and utilization. Thus, the theoretical model serves as an *a priori* model and guides the empirical research.

The empirical objective of the research is to observe the relational capital formation and utilization process as it unfolds within a real-life context, including exploring the interactions that take place between entrepreneurs and VCs as they react to the events and activities that occur during the process. Another objective is
to provide understanding of how the influential factors identified from five case studies of INVs in Finland affected relational capital formation and utilization. The outcomes of the relational capital process for new venture internationalization as found in the case studies help to inform the empirical model.

As suggested earlier in the scope of the study, the relational capital process is divided into two stages: formation of relational capital in the pre-investment stage, and utilization of relational capital during the post-investment stage. To achieve the theoretical and empirical objectives, two main research questions govern this study:

1) How do INVs develop and utilize relational capital as a means of obtaining venture capital investment for new venture internationalization?

2) How is relational capital between INVs and VC firms utilized for new venture internationalization after the venture capital investment agreement has been signed?

These research questions are both theoretical and empirical in nature. The first question “How do INVs develop and utilize relational capital as a means of obtaining venture capital investment for new venture internationalization?” aims to identify the influential factors affecting the formation of relational capital between INVs and VC firms. The motivation for building relational capital is different for the entrepreneur and venture capitalist, and the factors that affect formation of relational capital for each party may also be very different. The research question not only emphasizes the entrepreneurs’ actions in continuously developing relational capital with VCs to successfully raise venture capital for early internationalization, but also takes into consideration the VCs’ viewpoints. The answer to this first research question explores the role and clarifies the importance of relational capital for raising venture capital.

The aim of the second research question focusing on post-investment activities is to investigate the outcomes for INVs of relational capital formation, as well as how relational capital has been utilized for the new venture internationalization process. In the post-investment phase, VC firms have been known to become active equity owners that often sit on the board of directors and actively participate in decision-making for their portfolio firms (Fried et al. 1998, Zahra & Pearce II 1989).

Early internationalization often is related to liabilities, limited resources, and legitimacy problems for the INV. Therefore, pursuit of the answer to the second research question also will focus on value-added services that VC firms bring to
INVs in the new venture internationalization process through the utilization of relational capital in the post-investment phase, such as solving resource constraint problems and adding legitimacy to an as yet untested venture. Also in the post-investment stage, value-added services by VCs can establish relational capital with third parties, which can help to overcome the entrepreneurs’ liabilities associated with early internationalization.

Risk and uncertainty as perceived by entrepreneurs may be quite different from the perception of VCs, due to the VCs’ prior experience and knowledge of markets. While differences exist between the perception of VCs and entrepreneurs, strategies will be shaped by both of them, and changes in both strategy and perception may happen during the early internationalization process. These changes in strategy related to business routine, business model, innovation, and choice of foreign markets also will be affected by joint decisions between VCs and entrepreneurs.

None of the prior studies has discussed relational capital-related outcomes for the new venture internationalization process. Therefore, the second research question will fill this research gap by exploring relational capital utilization by VC-backed INVs during their internationalization process.

1.3 Key concepts

The key concepts of the study are defined below and offer a variety of perspectives and approaches.

Relational capital

“Relational capital” as defined for the purposes of this study is the level of trust and transparency developed in the course of interactions between INVs and VC firms that leads to positive venture capital decisions and value creation for new venture internationalization.

International new ventures (INVs)

In the international entrepreneurship academic discipline, related studies such as “International New Venture” (McDougall & Oviatt 1996), “Born Global” (Knight 1996, Madsen & Servais 1997), and “Global Start-ups” (Oviatt & McDougall 1995) emphasize the phenomena of early and rapid internationalization shortly after inception. For the purposes of this study, INV refers to a venture established by an
entrepreneur with the intent to internationalize early and quickly, within six years of inception, regardless of the foreign sales level.

**Venture capital (VC)**

“Venture capital” is defined as the investment by professional investors (often called venture capitalist, or VCs) of long-term, unquoted, risk equity finance in new ventures where the primary reward is an eventual capital gain supplemented by dividend yield. The focus is primarily on formal venture capital as early stage finance, frequently with a high-growth, high-risk, often high-technology aspect. Venture capital is invested in the form of equity rather than debt incurred by the entrepreneur.

### 1.4 Methodological approach and empirical setting of the study

This study adopts critical realism as a philosophical standpoint to investigate the relationship between INVs and VC firms. Critical realism has been widely applied to capture the complexity of business relationships and networks over time (e.g., Easton 2010, Morais 2011, Sousa 2010). The critical realism approach enables the researcher to critically investigate the conditions in which things stayed the same or changed over time. The critical realist acknowledges the dynamic nature of business structures, which changes based on continuous human agency (Easton 2002, Sayer 1992). In this study, the aim of applying critical realism is to explore and investigate events and activities that affect the relational capital formation and utilization process between INVs and VC firms, and the actions taken and changes made by entrepreneurs and VCs in reaction to those events and activities (Dubois & Gibbert 2010).

Järvensivu and Törnroos (2010) point out that critical realism often adopts a research logic based on abductive reasoning, which employs a “back-and-forth” approach to inquiry. Abductive reasoning focuses on the interplay between theory and empirical data (Dubois & Gibbert 2010). This particular study develops the theoretical model inducted from the current literature and serves as an *a priori* model for guiding the empirical data collection. In data analysis, the empirical model is built based on the data collected and discusses the emerging issues grounded in the real-life context. The theoretical model will be revisited in the discussion section by comparing the empirical model based on the data. Finally, a
conceptual model will be constructed by combining the theoretical and empirical models.

A multiple qualitative case study has been chosen as a research method. In this study, the cases serve as the context through which the qualitative data from entrepreneurs and VCs is collected. Next, all entrepreneurs’ viewpoints are summarized and compared with the VCs’ collective thinking. The qualitative data provides a rich description of the relational capital formation and utilization process from the point of approaching venture capital until exit (if any) and allows the interviewees to describe their emotional feelings, behavior, reactions, and decisions during the process of forming and utilizing relational capital. This is not a typical multiple case studies allowing to within case analysis, as not all the VCs from case companies can be reached. The selected cases serve as a context through which the entrepreneurs’ and VCs’ opinions and ideas are gathered. The multiple case studies make cross-case comparisons possible, and the collective understanding of the topic from both entrepreneurs and VCs increases the validity and reliability of the research.

The empirical evidence was collected in Finland, which provides an excellent setting for this study. First, given the typically short time frame from establishment of a venture to the time of first export activity, the relatively small size of the Finnish domestic market, and the fast-moving product life cycle (Luostarinen 1980, Luostarinen 1994, Luostarinen & Gabrielsson 2004), Finnish new ventures must rely on export to multiple markets from early in their inception. Early internationalization has become an important strategic choice for these new ventures.

Second, Finland is a small, open economy that has a well-established and active innovation policy (Autio & Yli-Renko 1998). In 2012, small and medium-sized enterprises with fewer than 250 employees represented 99.8% of all enterprises, employed 64% of the workforce, and accounted for 53% of turnover in Finland (Statistics Finland 2012). These facts support the notion that high-tech entrepreneurial new ventures have a strong impact on Finland’s national innovation system and economy. This degree of impact would not be possible in a larger economy.

Third, in recent decades, Finland’s Nokia was famous for competing on a global scale within the mobile phone industry. After Microsoft purchased Nokia’s Devices and Services business, there occurred a swift change in focus from high-growth mobile companies to entrepreneurial startups in Finland. Thousands of innovative entrepreneurial new ventures were established from 2008 to 2015.
Entrepreneurship is a significant strategy for fostering economic transformation of communities that are ravaged by the loss of industries due to globalization and out-sourcing (Nijhawan & Dubas 2007). To aid entrepreneurial activities, a number of public support organizations have been established to draw financial investment and nurture new ventures, such as Helsinki business hub and Butterfly Ventures in Oulu.

Fourth, access to financing represents one of the most significant challenges for entrepreneurs and for the creation, survival, and growth of newly established ventures in Finland. During the recession and the decline of Nokia and the paper industry, Finland attempted to attract venture capital as a means to support entrepreneurial activities and jolt the economy out of recession (Bloomberg, 2012). The latest VC-backed entrepreneurial firms that have attempted internationalization, Rovio Entertainment and Supercell, have created another generation of success stories for Finland. According to figures from the Finnish Venture Capital Association (2012), venture capital investing accelerates new ventures’ export intensity and increases the number of foreign board members. Those board members recommended by VC firms are more experienced in terms of age and the number of outside directorships. Venture capital has a strong social and economic impact by accelerating internationalization and growth in Finland. For these reasons, the Finnish context is a fertile resource for collecting rich primary research data for this study.

The empirical data draws from both entrepreneurs’ and VCs’ viewpoints while focusing on the process of raising venture capital for new venture internationalization in the pre-investment phase and utilization of relational capital in the post-investment phase. The interviewed entrepreneurs tell the full story of forming and using relational capital with VC firms, and VCs’ perspectives provide complementary data. The empirical data emphasizes the network or networking capabilities of entrepreneurs and their efforts in securing external equity funding for early internationalization through a course of interactions with VCs. It also reveals their feelings toward relational capital trend developed during the venture capital investment process. In terms of post-investment activities, the empirical data shows the outcomes or consequences resulting from the relational capital building process and its influence on INVs’ internationalization processes after venture capital involvement.

The INV subjects of the case studies are in high-technology industries that typically are attractive to VC investors. Due to the nature of the products, it often requires internationalization right after inception. The case study INVs included in
this research are located in the City of Oulu, where the research project was carried out. The close proximity of the case study INVs allowed for the establishment of a relationship with the interviewees and the ability to collect follow-up data whenever needed. In order to draw a clear picture of the importance of relational capital, the five cases were carefully selected to represent different situations, as described below.

Case one – Chaining: represents the thoughts of entrepreneur who ultimately abandoned venture capital as a financing option due to his reluctance to deal with the relationship aspect of involving VCs, but who still managed growth by other means of financing.

Cases two and three – Sending and Placing: represent current ventures that recently obtained venture capital for international business development and that have ongoing interactions with VCs. Sending and Placing offer a fresh perspective on the role of relational capital between INVs and VC firms.

Case four – Viewing: an older venture that has successfully raised three rounds of venture capital investment and has undergone an exit from the venture capital process.

Case five – Basing: this company successfully raised venture capital, but failed to exit due to the failure of the relationship with the VC firm.

These purposely-selected cases representing five distinct situations provide a complete picture of the relational capital formation and utilization process between INVs and VC firms, as well as the importance of relational capital in the INV/VC firm relationship.

1.5 Planned contribution of the study

This study contributes to existing INV literature by investigating the formation and utilization of relational capital between INVs and VC firms for new venture internationalization. In the discussion relating to INVs, much effort has been expended on studying the importance to entrepreneurial firms of relationships, but little is known about how entrepreneurs find, develop, and use different types of relationships to support internationalization (Sigfusson & Harris 2013). Financing is a key issue in the creation of entrepreneurial firms (e.g., Lockett et al. 2005, Ndonzuau et al. 2002, Schwienbacher 2007), and venture capital is considered an important source of funding for high-risk technological ventures.

As prior research indicates (e.g., De Clercq et al. 2006, Hsu 2006, Sapienza et al. 2006, Tyebjee & Bruno 1984), venture capital not only provides financial
resources, but also management know-how that is important for the INV’s survival and growth. This study offers new insights into how INVs are able to raise and utilize venture capital to support early internationalization, including resolving resource constraints, overcoming liabilities associated with internationalization, and leveraging needed resources by forming, developing, and utilizing relational capital with VC firms.

This study takes the relational capital viewpoint as a means of exploring the INV/VC firm relationship and considers the venture capital investment process one of building and using relational capital. The conceptual model that is constructed illustrates financing of entrepreneurial INVs as a process of turning relational capital into venture capital. The conceptual model categorizes the INV-related factors, VC firm-related factors, and human behavior-related factors that affect the formation of relational capital. It then determines the relational atmosphere within which relational capital is used for INV internationalization, via the sharing of both tangible and intangible resources between entrepreneurs and VCs. In addition, the study illustrates how an inadequate relational atmosphere may lead to relationship failure, resulting in the INV not obtaining venture capital or having an unsuccessful exit after venture capital investment.

Relational capital has been found to be important for raising venture capital (Liao & Welsch 2005). However, how relational capital works and its impact on post-investment activities still demands systematic research. This study solves this research problem by identifying INV-, VC- and behavior-related factors as being important for forming relational capital, and it also demonstrates that the associated relational atmosphere is related to the performance of INV internationalization after venture capital investment. Hence, the study offers new insight to the social capital theory by studying the role of relational capital as one social capital dimension at play in the INV and VC firm’s relationship.

The strong empirical foundation of this study suggests managerial implications for entrepreneurs who wish to raise venture capital for INVs. The entrepreneur should be aware of the factors that influence the formation and utilization of relational capital. For their part, VCs should be able to find a balance between a rigorous evaluation process and the behavioral factors that keep entrepreneurs motivated after venture capital involvement. For policy makers, the study emphasizes the role of referrals in helping INVs raise venture capital and the importance of signaling effects to VC firms. Public support organizations should arrange events and activities, such as “Money talks” and “Slush” pitching events, as well as offer incubating services related to new venture internationalization to
increase the valuation and credibility of INVs as being investment-ready candidates for VC firms.

1.6 Structure of the study

The introduction describes the theoretical setting of the study, including the introduction of relational capital as an approach to the study’s scope. Chapter 1 describes the theoretical and empirical objectives and formulates the research questions underlying this study. Chapter 1 continues with the empirical setting of the study, its planned contribution, and a description of the structure of the study.

The second and third chapters frame the relevant literature. Chapter 2 provides background knowledge on international new ventures, particularly from the network approach, and outlines the venture capital investment process as the research context. The chapter begins with a literature review regarding INVs that covers drivers of new venture internationalization and the related liabilities, challenges, and risks, as well as the importance of networks early in the internationalization process.

Venture capital investment as a research context is also introduced. The venture capital investment process, selection criteria, pre-investment and post-investment stages, and entrepreneur/VC firm relationship are presented to build the basis for the next chapter, “Theoretical framework of relational capital in venture capital process for new venture internationalization.”

Chapter 3 starts with a definition of relational capital in the context of venture capital and discusses how relational capital between INVs and VC firms is built, developed, and utilized for new venture internationalization. Following the venture capital decision-making process, the role of relational capital is clarified by identifying the four phases of this process: deal origination, screening, evaluation, and structuring. Next, the prior literature on potential changes and outcomes achieved by relational capital for new venture internationalization is described and analyzed. Chapter 3 also builds a theoretical framework for the empirical study which follows.

The fourth chapter discusses the research method, which involves adopting critical realism as a philosophical viewpoint for the study. The research takes a multiple case study approach and investigates five INVs that have been working with VC firms. This chapter also explores how these five INVs were selected, describes the process of data collection, and provides details about interviewees to
demonstrate the validity of the study. Chapter 4 ends with an introduction to the data analysis, which is based on the thematic coding strategy.

Interpreting and analyzing the collected data is an essential part of Chapter 5. This chapter begins with an introduction to the background of each case and continues by describing each INV’s experience with forming and using relational capital with their VC firm. Next, examples are offered to illustrate VCs’ collective understanding of relational capital formation and utilization. Similarities and differences how entrepreneurs and VCs view relational capital related to relational capital between entrepreneurs and VCs are summarized and discussed. Chapter 5 analyzes each key factor that influences formation and utilization of relational capital in this INV-VC context, as well as adds emerging issues revealed by the data that potentially influence how relational capital for new venture internationalization is formed and used by INVs and VC firms. Finally, an empirical model is presented based on the findings and results.

Chapter 6 summarizes the research results and draws conclusions based on the findings. The chapter begins with an overview and discussion of the findings and continues to answer the two main research questions by reflecting on this study’s results compared to the prior literature.

Chapter 7 discusses the theoretical contribution to INV, VC and social capital literature and managerial implications for entrepreneurs, VCs, and policy makers. Chapter 7 further outlines the limitations of the study and potential future research directions. The dissertation ends with Chapter 7’s summary of the research process and general conclusions of this study. This study is written as a monograph that includes the seven chapters as illustrated in Figure 2.
Fig. 2. Outline of the study
“Getting to know the unknown through the known”

– Confucius
2 INVs, venture capital, and internationalization

This second chapter reviews the literature that is related to INVs and network relationships and describes the venture capital investment process as a research context for this study. The reviewed literature in Chapter 2 provides the basis for discussion on relational capital between INVs and VC firms and develops a theoretical model of this study in Chapter 3. The chapter starts by introducing INVs and the liabilities associated with new venture internationalization, as well as describing the role of entrepreneur as a decision-maker. The literature review continues with a discussion of the venture capital investment process. More specifically, the venture capital process is clarified in terms of describing each stage of the decision-making process and the activities related to portfolio firms, such as monitoring and value-added services. Finally, research related to venture capital and new venture internationalization is further highlighted and reviewed.

2.1 International new ventures

The phenomenon of INVs that internationalize shortly after inception has been extensively studied in the field of international entrepreneurship (e.g., Jones & Coviello 2005, Jones et al. 2011, Oviatt & McDougall 2004a, Oviatt & McDougall 2004b, Oviatt & McDougall 2005). Apart from the prevailing Uppsala internationalization model, which studies the incremental internationalization process in multinational companies (Johanson & Vahlne 1977), studies of firms such as “International New Venture” (McDougall et al. 1994), “Born Global” (Knight 1996, Madsen & Servais 1997), and “Global Start-ups” (Oviatt & McDougall 2005) emphasize the phenomenon of early and rapid internationalization (Oviatt & McDougall 2004). This study follows the broader and well-accepted definition of early internationalization provided by Oviatt and McDougall (1994:50): “A business organization that, from inception, seeks to derive significant competitive advantage from the use of resources and the sale of output in multiple countries.”

Most scholars interpreted McDougall’s “from inception” as referring to INVs that internationalize within a few years of establishment, typically among firms that are six years old or younger (Knight & Cavusgil 2004, Shrdar et al. 2000, Zahra et al. 2000, Zahra 2004). Thus in this study, INV is defined as a firm established by the entrepreneur with the intent to internationalize within the first six years of
existence. McDougall (1994) defines internationalization as “use of resources and sale of outputs in multiple countries,” while others measure “internationalization” in terms of intensity, percentage of international sales (Reuber & Fischer 2002), scope of internationalization (Preece et al. 1999), activities and engagement in foreign markets (Bloodgood et al. 1996), international sales growth (Autio et al. 2000), and type of internationalization (Kuemmerle 2002). In this study, internationalization focuses on a new venture that successfully enters into a foreign market to develop sales potential. Having clarified “from inception” and “internationalization” from other perspectives, the definition of INV for the purposes of this dissertation is a new venture that successfully enters into a foreign market within six years of inception, regardless of the foreign sales level.

Internationalization has become an important strategic decision for both large multinationals and entrepreneurial startups in today’s economy (Zahra et al. 2005). Apart from the prevailing Uppsala internationalization model studying the incremental internationalization process in multinationals (Johanson & Vahlne 1977), INV research is closely related to the discipline of international entrepreneurship. The Uppsala model describes a slow and gradual process of internationalization. At the firm level, the Uppsala model of internationalization explains that foreign market entry decisions are determined by the necessary progressive accumulation of knowledge related to the entry and commitment of resources in foreign markets.

To minimize risks and deal with uncertainty, foreign market entry modes are a succession of stages beginning with an export activity, continued by contractual agreements, and finally achieving direct foreign investment from countries that are physically or culturally close to the distant areas (Johanson & Vahlne 1977, Johanson & Vahlne 1992). Rooted in firm-level analysis, the Uppsala process theory of internationalization somewhat neglects the value of entrepreneur as decision-maker as well as his/her prior experience and personal network resources and knowledge. It also tends to neglect the significance of small domestic market size and the impact of sophisticated communication technologies.

In the international entrepreneurship domain, internationalization is conceptualized as an entrepreneurial act that involves the process of identifying, evaluating, and selecting from a variety of markets where the competitive advantage of the new venture can be maximized (Ellis 2010, Jones & Coviello 2005, Lee & Park 2006, McDougall & Oviatt 1996). Internationalization involves a series of important entrepreneurial decisions regarding how to explore, enact, evaluate, and exploit opportunities that create future goods and services across national
borders (Oviatt & McDougall 2005) or match existing goods and services to launch into new markets (Ellis 2010).

New venture internationalization has several advantages. McDougall et al. (1994) argue that new ventures may utilize unique core competencies (e.g., innovation, technology, culture, relationships) to gain access to various resources without owning them, and thus can quickly build better competitive advantage over rivals. Autio et al. (2000) show that new ventures may achieve performance advantages since they enjoy learning advantages over established multinationals. Similarly, Zahra et al. (2000) and Zahra (2005) propose that new ventures are more adapted to learning technology in international markets, which influences venture growth and profitability and finally increases the return on the resources engaged in the foreign markets.

Expanding into new overseas markets represents a potential opportunity for value creation as well as growth and return on resources when the new ventures leverage resources in different markets and enter into positions to capitalize on market imperfections (Lu & Beamish 2006). Prior studies have also indicated that new ventures may benefit from early internationalization to enjoy learning advantages (Autio et al. 2005, De Clercq et al. 2012, Zahra et al. 2000), enhance financial performance (Lu & Beamish 2001, Sapienza et al. 2006), and develop innovations (Kafouros et al. 2008, Knight & Cavusgil 2004). Sapienza et al. (2006) show the positive correlation between survival and growth of a new venture.

In order to understand what have been contributed to achieve internationalization advantages during the new venture internationalization process, researchers have made efforts to study cross-border entrepreneurial activities related to the importance of knowledge (Johanson & Vahlne 1977), learning (Autio et al. 2000, De Clercq et al. 2012, Fernhaber et al. 2009), network relationships (Coviello & Munro 1997, Coviello 2006, Fernhaber & Li 2013), industry structure (Fernhaber et al. 2007), and human capital of the entrepreneur or top management team (Isidor et al. 2011, Prashantham & Dhanraj 2010, Prashantham & Young 2011) in the internationalization process.

Internationalizing INVs with scarce resources that are operating in niche markets and that have limited presence and capabilities (Weerawardena et al. 2007), and often involves a set of challenges in foreign markets, particularly related to several types of internationalization liabilities: liability of newness (Nagy et al. 2014, Stinchcombe & March 1965), liability of inexperience (Zahra 2004), liability of smallness (Freeman et al. 1983, Kale & Arditi 1998), liability of foreignness (Zaheer 1995), and liability of outsidership (Johanson & Vahlne 2009). Any of
these liabilities may hinder new ventures from achieving profitability or may even endanger their survival in foreign markets.

The liabilities of newness and inexperience hinder new ventures that are trying to obtain valuable resources in existing networks. The third liability relates to the small size of new firms, which challenges the survival of the new ventures’ internationalization processes. The fourth liability results from “foreignness” that builds barriers to international market entry and makes it more difficult to access potential suppliers and customers. The fifth liability faced by new ventures is outsidership, as the internationalization process for new ventures can be defined as a by-product of the entrepreneurs’ attempts to identify and develop opportunities in their existing networks (Schweizer et al. 2010).

2.1.1 Entrepreneurs in international new ventures

A broad definition of international entrepreneurship is related to opportunity recognition and exploitation. Caligiuri et al. (2004) argue that it is important to understand entrepreneurs’ collective attitudes toward organizations and their impact on internationalization of firms (Sullivan 1994). Entrepreneurs who are willing to be involved in international markets have the propensity for risk-taking, innovation, and proactivity, and subsequently these features increase the likelihood of venture success.

George et al. (2005) also argues that entrepreneurs are willing to accept additional risks associated with the internationalization of the new venture only to the extent that such risks are accompanied by potential benefits, or that the additional risks can increase the return on their investment. New venture internationalization that may lead to the loss of entrepreneurs’ wealth, careers, and reputation from the agency perspective (Eisenhardt 1989a). Pursuing internationalization as a strategy before obtaining external venture capital equity financing indicates the confidence, motivation, and risk-taking spirit of the entrepreneurs, as foreign expansion is a costly and risky activity.

Entrepreneurs play a central role in decision-making for the internationalization process by acting on international opportunities and assessing risks and returns that accompany this process. Prior literature has described that an entrepreneur’s internationalization decisions center around his or her experience, knowledge, and network relationships (Reuber & Fischer 1997, Ruzzier et al. 2007). Entrepreneurs’ different decisions regarding opportunity exploitation depend on the type of uncertainty they have experienced, including prior entrepreneurial ventures.
Both the serial entrepreneur’s past ventures and current portfolio are important path-dependent resources to formulate current strategies. These earlier experiences lead to further refinement of identified opportunities and/or identification of new opportunities, and finally to subsequent internationalization acts and decisions.

The background of the entrepreneur (i.e., personal experience, knowledge, and network relationships) (Ghannad & Andersson 2012) affects how any new activity is viewed and, subsequently, shapes the current view of decisions regarding foreign market entry. For example, well-educated entrepreneurs who are internationally experienced and masters of foreign languages may exhibit a positive attitude toward internationalization, have a high tolerance for physical distance, and prefer to enter international markets where they have been working or studying (Freeman & Cavusgil 2007). Prior experience in international markets evidently influences the appraisal of early internationalization (Reuber & Fischer 1997).

Social networks obtained from previous employment may help provide information to evaluate foreign market barriers (Santos-Álvarez & García-Merino 2010), and reduce setup costs stemming from lack of organization experience in internationalization (Cooper & Dunkelberg 1986, Sapienza et al. 2006). In this way, the entrepreneurs themselves may be more willing to accept additional risks associated with new venture internationalization, especially when foreign markets are familiar to them (McDougall et al. 2003). Overall, the entrepreneur plays a central role in leading the direction of international market exploration and exploitation.

### 2.1.2 Network relationships of international new ventures

“Markets are networks of relationships in which firms are linked to each other in various, complex, and, to a considerable extent, invisible patterns.” (Johanson & Vahlne 2009: 1411). International entrepreneurship research provides an increasingly deep understanding of the importance and value of international business relationships and emphasizes the fundamental importance of network relationships for international market exploration and exploitation, especially for small, new, high-tech ventures (Coviello 2006). Given the fast obsolescence of products, limited domestic demand (Crick & Spence 2005), and “resource poverty” of new ventures, cooperative networks and business in international markets become important for growth and survival of new ventures.

The initial network relationship of a new venture depends on the social contacts of management teams (Agndal et al. 2008, Zeng et al. 2009) and gradually moves
to developed secondary networks with other firms (Mort & Weerawardena 2006). The internationalization process of a new venture can be seen as a process of initiating, establishing, managing, and developing international network relationships (Johanson & Vahlne 2006). Network relationships act as conduits, providing valuable resources to increase foreign strategic alternatives and opportunities.

The existing network relationships of a firm determine the opportunities available in a particular period (Johanson & Vahlne 2006), and the amount of relationships determines the diversity of knowledge and information to evaluate and act upon the available alternatives and opportunities (McDougall et al. 1994). In accordance with Johanson and Vahlne (2006), this dissertation is based on the assumption that entrepreneurs and their new ventures are embedded in both social and business relationships to develop international business.

In the context of INV creation, Mainela and Puhakka (2011) argue that the emergence of INVs relates to an international opportunity that evolves and is revisited over time in the networks through the entrepreneurial networking process. For developing INVs, the networks’ roles are multiple. The network relationships are sources of access to tangible (e.g., venture capital investment) and intangible resources held by the other party. Such benefits and advantages obtained by INVs through network relationships may accelerate the innovation process, increase the capability for continuous learning, combine some specific functions shared with others, stimulate scale economies, and help to anticipate trends and changes within the society for new market opportunities.

The provision of market information and knowledge by inter-organizational relationships is a key benefit of networks for the entrepreneurial process and contributes to knowledge-building of new ventures. Information and advice obtained from exchanging relationships facilitates foreign market entry, developing international business routines and reducing high setup costs of internationalization (Agnadal et al. 2008, Zeng et al. 2009). The expertise of third parties in a relational network may influence the appraisal of foreign market barriers (Cooper & Dunkelberg 1986, Sapienza et al. 2006) and help entrepreneurs to partially avoid risks of internationalization arising from the liability of inexperience.

Gaining a reputation and endorsement from network partners has positive signaling effects to the markets of the resource provider (Lechner et al. 2006) and helps new ventures to offset internationalization liabilities of newness and smallness (Shane & Cable 2002). Entrepreneurs’ networks for information,
resources, and knowledge affect the outcomes of any new venture (Johanson & Vahlne 1977).

The internationalization process begins with seeking foreign market opportunities and obtaining relevant market information. The market-entry information regarding markets and opportunities depends heavily on the network of the firm and on the social networks of the management teams (Agndal et al. 2008, Zeng et al. 2009). The expertise of other firms and third parties in a relational network may help entrepreneurs avoid some of the risks of internationalization and improve the international performance of the firm (Agndal et al. 2008). Zeng et al. (2009) noted that networking and knowledge-based activities should be employed to improve management experience and achieve internationalization and success in international business. Indeed, continuous increase of experience in international markets leads to greater knowledge and confidence in relationship decisions (Coviello & Munro 1997).

New ventures usually engage in relationships with larger firms in an international network to develop their products. Involvement in these networks enables the new venture to achieve market entry and knowledge about the business world, and thus gradually increases market visibility. In turn, this may make the new venture a candidate for acquisition by another firm within its network (Coviello & Munro 1997). In line with prior research (see Coviello & Munro 1997), Kiederich and Kraus (2009) argue that the internationalization of new technology-based firms may increase the chances of becoming acquired. In practice, VCs are more willing to invest in new ventures that have already shown clear exit potential, either through initial public offering or acquisition. New ventures that manage to improve their network positions by utilizing relational capital in international markets positively affect venture capital investment decisions.

To summarize the foregoing discussions, it is important for INVs in the early phase to build, develop, and utilize relationships to obtain tangible and intangible assets for development. This dissertation investigates the INV and VC firm relationship in detail and its importance for the development of INVs.

### 2.2 Venture capital investment and process

Venture capital is a major source for funding technology-intensive new ventures at the early stages of their development. These firms are typically young, represent high risk levels, and show potential for high returns, but are plagued by a high degree of uncertainty as a result of the untested and unproven nature of their
products, technology, and business model (Kaplan et al. 2009). VC firms usually buy the shares of young firms in the form of equity financing, but sometimes debt arrangements or a combination of two forms (including preferred stock and convertible securities) can also be provided by the VCs (Landskroner & Paroush 1995). Entrepreneurs contribute “entrepreneurship,” sometimes referred to as “sweat equity,” and provide the initial financing for the new venture. Venture capital has been proven one of the most important financial capital sources for high-technology startups (Gupta & Sapienza 1992). VC firms recycle their investment through initial public offerings, which represent the majority of venture capital returns, followed by acquisition.

Often, venture capital investments take place after the founders’ self-financing is running out but while the firms are still privately held (Landskroner & Paroush 1995). VC firms normally focus on early-stage ventures that have drafted a realistic business plan and conducted some basic market research on the initial product or service, but typically have not yet generated revenue (Ruhnka & Young 1987). Those uncertainties contribute to VCs’ perception of much higher risks associated with making investment decisions on early-stage ventures with non-commercialized products, unproven technology, and untested markets, than on later-stage companies which have well-developed products and a defined market (Dimov et al. 2007, Podolny 2001, Ruhnka & Young 1987).

The venture capital investment process is often considered to consist of multiple stages: deal origination, screening, evaluation, structuring, and post-investment activities (Hall & Hofer 1993, Tyebjee & Bruno 1984) from the time the venture proposal is received until the point when the VCs ultimately take profits from the venture through exit, preferably in the form of initial public offering (Kaplan & Strömberg 2005). Building upon the existing literature (Fried & Hisrich 1994, Hall & Hofer 1993, Meyerson & Agge 2008, Proimos & Wright 2005, Tyebjee & Bruno 1984), the venture capital investment process can be segmented into the pre-investment phase – before any venture capital allocation decision – and the post-investment phase, which occurs after the capital is allocated to the funded venture.

2.2.1 Pre-investment phase

The pre-investment venture capital decision-making process includes multiple sequential stages: deal origination, screening, evaluation, and structuring (Hall & Hofer 1993, Tyebjee & Bruno 1984). Deal origination is the process that considers
deals as investment prospects (Tyebjee & Bruno 1984). Screening is the process in which received proposals are quickly scanned in terms of investment size, policy, industry, location, and the stage of financing. In screening, the number of investment proposals is reduced to a manageable level for in-depth evaluation (Bengtsson et al. 2002, MacMillan et al. 1987, Tyebjee & Bruno 1984, Wells 1973). Deal evaluation is the process of assessing the perceived risk and expected return based on selection criteria, followed by a decision whether to invest in the venture (Baum & Silverman 2004). The deal structuring phase includes negotiation of the price of the deal and drafting of the formal investment contract that assigns control rights and obligations (Bengtsson & Sensoy 2011, Kaplan & Strömberg 2003a, Kaplan & Strömberg 2005, Norton 1995, Williams et al. 2006). In general, a rigorous venture capital decision-making process serves to reduce investment risks and protect the shareholders’ interests.

Table 1. Literature review of key venture capital investment criteria

<table>
<thead>
<tr>
<th>Venture capital decision criteria</th>
<th>Main indicator</th>
<th>Relevant literature</th>
</tr>
</thead>
<tbody>
<tr>
<td>Characteristics of entrepreneur/Team</td>
<td>experience</td>
<td>Patzelt 2010, Roure &amp; Maidique 1986</td>
</tr>
<tr>
<td>Market characteristics</td>
<td>timing of entry</td>
<td>Shepherd et al. 2000</td>
</tr>
<tr>
<td></td>
<td>customer</td>
<td>Kaplan &amp; Strömberg 2000</td>
</tr>
<tr>
<td></td>
<td>competitive rivalry</td>
<td>MacMillan et al. 1987, Shepherd 1999</td>
</tr>
<tr>
<td>Product characteristics</td>
<td>market acceptance</td>
<td>Petty &amp; Gruber 2011</td>
</tr>
<tr>
<td></td>
<td>differentiation</td>
<td>Petty &amp; Gruber 2011, Tyebjee &amp; Bruno 1984</td>
</tr>
<tr>
<td></td>
<td>technology</td>
<td>De Cleyn &amp; Braet 2007, Fried &amp; Hisrich 1994</td>
</tr>
<tr>
<td></td>
<td>expected risk</td>
<td>Poindexter 1976, Shepherd 1999</td>
</tr>
<tr>
<td>Network characteristics</td>
<td>alliance/strategic partners</td>
<td>Baum &amp; Silverman 2004, Shepherd 1999</td>
</tr>
</tbody>
</table>

The high failure rate of venture capital investments (Timmons & Bygrave 1986) has compelled the venture capital industry to establish a rigorous selection process prior to investment (MacMillan et al. 1986, Tyebjee & Bruno 1984). Accordingly,
controlling the pre-investment process in terms of selection is extremely important in securing positive returns on venture capital investments (MacMillan et al. 1986, Muzyka et al. 1996, Shepherd 1999, Tyebjee & Bruno 1984, Wright et al. 2005).

Table 1 summarizes the funding selection criteria into five parameters and maps important indicators into those parameters for future analysis. Venture capital literature suggests that each evaluation made by VCs of a specific investment proposal is primarily determined by the entrepreneurs’ or the entrepreneurial teams’ capability (Chen et al. 2009, Franke et al. 2008, Kaplan & Strömberg 2005, MacMillan et al. 1986, Robinson 1988), market and competitive environment (Dos Santos et al. 2011, Mason & Stark 2004, Muzyka et al. 1996, Tyebjee & Bruno 1984, Zacharakis & Meyer 1998), and product attractiveness (Clarysse et al. 2005, Meyerson & Agge 2008).

### 2.2.2 Post-investment phase

New ventures that have received venture capital perform better than those of non VC-backed firms in terms of increased sales, employment, and productivity growth (e.g., Croce et al. 2013, Cumming et al. 2014). VC firms play a significant role in professionalization of new ventures (e.g., Christofidis & Debande 2001, De Clercq et al. 2008, Ehrlich et al. 1994, Fried et al. 1998). Beyond provision of financial capital, venture capitalist’s role includes “monitoring” and “value-added services” (De Clercq & Manigart 2007). Due to the limited lifespan of venture capital funds, the venture capital process lasts up to seven years from the investment decision through exit for return on investment. The performance of portfolio firms strongly influences the performance of VCs and their ability to secure future investment pools (Sahlman 1990). Therefore, VC firms spend a tremendous amount of time nursing portfolio firms and making decisions regarding current and future questions about the venture’s direction. VCs often sit on the board of the new venture to guide the direction of financial and strategic discipline. A significant board representation gives VCs the right to replace underperforming key staff, or even the entrepreneur, in VC-backed new ventures, which is most likely to happen when forecasted time-to-exit is short (Gerasymenko & Arthurs 2014). Entrepreneurs should report to their VC firms in regularly arranged board meetings (Fried et al. 1998) regarding milestones that have been set and achieved (Hellman & Puri 2000).

A significant amount of the studies has investigated under what conditions VC firms add the greatest value to their portfolio firms. Venture capitalist’s value-added services in the post-investment phase provide portfolio companies with operating
services, valuable business contacts, market knowledge, know-how, and industrial experience (Fried & Hisrich 1994). De Clercq et al. (2006) summarize different roles that VC firms play in invested new ventures, including strategic, financing, networking, interpersonal, reputational, and disciplinary roles. VCs use either a “hands-on” or “hands-off” approach to monitoring operating performance depending on the developmental phase of the new venture.

VC firms have a range of network contacts linking new ventures to potential customers, suppliers, financiers, and experienced managers, up to and including the VC firm’s own syndicate of portfolio firms (Pratch 2005). As a mentor, friend, and confidant to the entrepreneur, a venture capitalist also provides moral support for entrepreneurs and top managers to deal with uncertainty, stress, misgivings, and doubt (De Clercq et al. 2006, Pratch 2005).

INVs are often associated with the liabilities of newness and inexperience. Initial legitimacy of INVs comes from the entrepreneur’s active involvement in and interaction with an existing social structure and establishment of reliable relationships (DiMaggio & Powell 1983, Suchman 1995, Zimmerman & Zeitz 2002). Another important means of INVs gaining local or international presence is to be endorsed by respectable organizations such as VC firms. Obtaining venture capital investment provides a strong signal of an INV’s quality and future prospects (Podolny 2001, Stuart et al. 1999). Affiliation with a famous VC firm increases the INV’s IPO valuation. The legitimizing role of VC firms is especially important for INVs that are subject to great uncertainty (Amit et al. 1998). Legitimacy provided by a VC firm with a solid reputation helps a startup to access more resources, which enables the new venture to overcome the liability of newness (Chang 2004, Zimmerman & Zeitz 2002).

VC firms function in a disciplinary role in cases of founder/CEO replacement. The founder replacement often occurs in early-stage investment stage, shown over 30% in Wasserman (2003)’s study and 40% in Kaplan et al. (2009)’s study. Providing value-added advice requires considerable time and effort. Therefore, if the expected time-to-exit is short, VCs would prefer to replace a founder with an experienced one chosen from their network, or one found by headhunters. Replacing the CEO could potentially add missing knowledge and a new network, which may reduce the level of effort and attention required of VC firms for advising (Gerasymenko & Arthurs 2014).

For many VCs, the preferred exit route is IPO, followed by trade sales. IPO brings a higher valuation for new ventures than a trade sale. An IPO raises additional equity capital from the public market for the future operation, and the
entrepreneur remains as CEO of the firm, even though his or her equity ownership decreases as a result of the IPO. Conversely, trade sales provide immediate, full liquidity to both entrepreneur and venture capitalist. On the other hand, selling the new venture to a larger corporation results in the entrepreneur losing all control over the founded venture, up to and including being compelled to leave the company. In this case, the entrepreneur would also need to buy back the VC firm’s equity.

Upon exit from a funded venture, the VC firm can also choose liquidation as the exit method, in which the venture’s assets are sold for their salvage value. Liquidation results in loss of original investment by the venture capitalist and loss of financial investment, income, and a dream by the entrepreneur, because typically liquidation cannot pay off all investments (Sapienza 2006, Cumming & MacIntosh 2003, D’Aveni 2005).
Fig. 3. Summary of the venture capital investment process

To summarize these discussions on pre-investment, post-investment, and exit routes, Figure 3 illustrates the entire venture capital investment process, mapping all events and activities that the new venture and VC firm organize and undertake. As shown in Figure 3, the time frame of this study begins at the point of approaching venture capital until the point of exit, with focus on the activities undertaken by the two actors in the venture capital decision-making process and post-investment interaction. Planning, implementation, method, and execution of exits are outside the research scope.
2.3 Review of venture capital and portfolio ventures’ internationalization

Due to the increasing number of INVs eligible for venture capital investment, the phenomenon of venture capital ownership and new venture internationalization emerged as a popular topic for study early in the 21st century. INVs receive considerable financial and managerial support from VC firms under conditions of great uncertainty within international environments (Mäkelä & Maula 2005).

Some research has begun to shed light on this topic and has shown that venture capital involvement both positively and negatively affects new venture internationalization in various respects. Carpenter et al. (2003) argued that venture capital influences internationalization in high-technology IPO firms in situations where the venture capitalist is able to appoint an internationally experienced director to the board by using risk and control mechanisms. George et al. (2005) found that VCs motivate small- and medium-sized firms to expand their businesses internationally, but that they are not able to statistically support the relationship between venture capital ownership and international scale. Lipuma (2006) has made further research progress, empirically testing the notion that corporate VC firms increase the export intensity of portfolio firms in new venture internationalization. Lockett et al. (2008) confirmed that VCs’ value-added resources promote export behavior in early-stage ventures, and monitoring is a more effective way to promote export behavior in late-stage ventures.

To offset the liabilities of inexperience and newness of VC-backed INVs, Fernhaber and McDougall-Covin (2009) have demonstrated that reputable VC firms can serve as a catalyst to new venture internationalization by transferring international knowledge to the funded new venture and signaling the quality of the venture to external network partners, based on the resource-based view approach. Smolarski and Kut (2011) have studied the relationship between venture capital investment and export intensity of portfolio firms by looking at different investment methods: incremental financing and the lump-sum approach. Their research indicates that only incrementally financed and syndicated firms improve their export ratio compared to the lump-sum approach. This may be interpreted to indicate that close monitoring by VCs that sets milestones for new ventures and the network resources of the VC firm have a strong impact on portfolio firms’ export performance.

From the resource-based view, Zahra et al. (2007) have argued that VCs’ ownership contributes to building human capital and the proprietary types of
knowledge-based resources needed for internationalization of small- and medium-sized companies. Lutz and George (2012) have indicated that provision of slack financial resources itself positively relates to development of internationalizing new ventures. Further arguments in Lutz and George’s study hold that greater heterogeneity in the managerial resources of VCs, such as investment experience, entrepreneurial experience, and industry knowledge, contributes to the scale of internationalization of new ventures. Greater heterogeneity in the strategic resources of VC firms, which relates to access to their professional network, financial investors, industry players and executive recruiters, enables a degree of foreign market exploration. As strategic advisors (Sapienza et al. 2006), VCs who have international growth aspirations in turn increase the aspirations of entrepreneurs in international markets (Lutz & George 2012).

Other researchers investigate this phenomenon from the perspective of the internationalization of VC firms. Humphrey-Jenner and Suchard (2013) have argued that foreign VCs increase the likelihood that a portfolio company will list on a foreign exchange market, as connections to top-tier lawyers, investment banks, and accountants can facilitate international listing and overcome the liability of foreignness. The portfolio new ventures that focus on domestic market only and have less than six years old until the point of IPO can be considered as international new ventures when IPOs have been launched in foreign stock market.

Venture capital may also bring about a negative impact on new venture internationalization. As the venture capital industry itself has recently started to enter international markets and often lacks foreign investment experience and knowledge, the internationalization of their portfolios’ new ventures complicates the situation due to the limited abilities of the VCs to monitor distant operations (Lipuma 2012; De Prijcker et al. 2011). If VCs lack the knowledge and resources to support internationalization activities, the VC firm may hold internationalization in disfavor (George et al. 2005). In addition, Smolarski and Kut (2011) have revealed that an internationalizing firm may benefit from a VC firm’s efficient monitoring and risk management. However, too many restrictions also can lead to negative effects on internationalization activities and performance, as firms need operational flexibility to deal with the greater uncertainties surrounding international business operations.

The recent studies on venture capital and new venture internationalization approach the relationship from different angles. The debates in prior literature center around venture resources, control issues, and valuation of exit when considering whether VC firms should invest in early internationalization. The
mixed performance results of VC-backed early internationalization makes the phenomenon complex to understand.

Another stream of study focuses on the performance of internationalization by measuring the scope, scale, and speed of new venture internationalization after venture capital involvement. As introduced in Chapter 1, the instrument that affects the raising of venture capital for new venture internationalization and the internationalization performance of INVs has not yet been clarified. In Chapter 3, relational capital will be examined in terms of the role it plays for raising and utilizing venture capital, as well as to understand the relationship between the INV and VC firm.
“If you work hard enough at it, you can grind even an iron rod down to a needle”

– Chinese Proverb
3 Theoretical framework of relational capital in the venture capital process for new venture internationalization

In this chapter, the aim is to conceptualize relational capital and its implications within the venture capital context, and finally to build a theoretical framework for further empirical studies. The present chapter starts with introducing the prevailing and dominant approaches applied to analyzing the entrepreneur/venture capitalist relationship and provides reasoning for choosing relational capital as a lens through which to view this dyad relationship. Further effort is made to clarify the factors that affect the formation and utilization of relational capital between INV and VC firm from the point of approaching the venture capital firm until exit. This chapter concludes with a theoretical model that illustrates the role of relational capital in the venture capital investment process for INVs.

3.1 Points of view on entrepreneur and venture capitalist dyad relationship

In venture capital discussions, there are three dominant analytic approaches to research: agency theory (Jensen & Meckling 1976), stewardship theory (Donaldson & Davis 1991), and procedural justice theory (Sapienza & Korsgaard 1996). Agency theory is a given for analyzing the behavior of VCs and entrepreneurs, with its assumptions of self-interest, information asymmetry, and goal conflict. Self-interested behavior on the part of either the entrepreneur or venture capitalist can ruin the relationship (Cable & Shane 1997, Sahlman 1990, Sapienza & Korsgaard 1996). Agency theory suggests that the entrepreneur as agent takes the information advantage at their procession to act opportunistically at the expense of the venture capitalist or principal, and to pursue personal interests (Eisenhardt 1989a). VC firms also may act opportunistically in terms of time and effort allocation to a venture (Sahlman 1990), timing of IPO (Gifford 1997), and re-investment decisions. However, Arthurs et al. (2003) have argued that VCs’ and entrepreneurs’ goals tend to become aligned after investment allocation. Thus, without rationale for why the goals are incongruent, the agency theory fails to explain entrepreneurs’ and VCs’ behaviors in the post-investment phase. Nor does the agency theory take into consideration how the decision-making process affects the perception and resolution of the agency problem (Forbes & Milliken 1999).
Stewardship theory assumes that entrepreneurs simply abandon their self-interest to serve the venture capitalist’s goals and ignores the role of the entrepreneur’s vision or aspiration toward venture success (Santos-Álvarez & García-Merino 2010). Prior venture capital research was mainly built on agency theory, with insights from stewardship theory; however, the ability of these theories to provide a basis for understanding venture capital from the social-relational nature of venture capital investment has been challenged (Bruton et al. 2005, Shane & Cable 2002).

Procedural justice theory is concerned with fairness in decision-making (Colquitt et al. 2001, Luo 2007). This theory often informs the approach to investigating employer/employee relationships (Sahlman 1990). In the venture capital context, some researchers believe the procedural justice theory is equally applicable, because the funded new venture is dependent on the VC firm for important tangible and intangible resources it otherwise would not be able to obtain (Gomez-Mejia et al. 1990, Sapienza & Korsgaard 1996). Procedural justice theory suggests that entrepreneurs are more willing and likely to continue offering sweat equity when VCs treat them in a procedurally fair manner (Sapienza et al. 2000). This view helps us understand the role of trust and fairness in promoting the entrepreneur’s psychological ownership of the venture, over and above legal ownership. However, to some extent, the procedural justice approach neglects the unequal bargaining power of an entrepreneur who holds the information advantage over the venture capitalist.

The viewpoint of this study does not rely on regarding the dyad relationship in terms of opportunistic behavior, as suggested by agency theory, or as sacrificing the needs of the entrepreneur to serve the VC firm’s interests, as proposed by stewardship theory. This study adopts the procedural justice theory view, believing that the INV and VC firm’s relationship is positive, holistic, and cooperative. The relational capital approach used in this study acknowledges the power and voice of the entrepreneur and assumes the relationship between the INV and the VC firm is not one of dependence, but one of equality. The aim of this approach is to examine the role relational capital plays in raising venture capital in the initial funding phase, and how relational capital promotes a collaborative relationship, goal alignment, and value appropriation in the post-investment stage of the investment process.

Bygrave (1987, 1988) proposed that networks are important for U.S. VCs. Further exploration by Shane and Cable (2002) and Stuart et al. (1999) supports this view with a large sample survey. The influence and importance of networks on venture capital has received wide acknowledgment (e.g., Ahlstrom & Bruton 2006,
Sorenson & Stuart 2008) in the field, however, due to the dominance of agency and stewardship theories, it has not yet been widely applied in venture capital research. In this study, the investment process is seen as a network-building and utilizing process that adds value to both parties throughout the entire investment period.

### 3.2 Defining relational capital

Relational capital is value that is generated by building, developing, and maintaining good relationships within an organization’s operational environment with customers, suppliers, employees, governments, and other stakeholders (Adecco 2007). Prior studies mainly investigated relational capital in a defined context, such as alliance studies, the customer/supplier relationship, and entrepreneurial teams.

Relational capital refers to the value of the relationship an individual or organization has with its environment (Cousins et al. 2006, Gulati et al. 2002) or a set of relations that a firm has with various local actors or stakeholders in a given environment (Welbourne & Pardo-del-Val 2009). In the buyer/seller relationship, for example, relational capital can be simply interpreted as goodwill between customer and supplier, which is the extent of the definition of customer capital (Patricia Ordonez de Pablos 2003). Relational capital contributes to the success of new firms by resulting in repeat customers, thus building a good reputation with external stakeholders, including suppliers and financial entities. Additionally, even the support of an entrepreneur’s spouse or life partner can contribute to building good relational capital, especially in the initial phase of venture development (Hormiga et al. 2011).

Another stream of research rooted in social capital theory defines relational capital as the interpersonal connections in a network that have been developed through interactions based on trust and respect (Nahapiet & Ghoshal 1998). Relational capital is frequently discussed as one of three dimensions of social capital, relating to the particular quality of relations that an actor has and that influences his or her behavior (Nahapiet & Ghoshal 1998). In a similar vein, relational capital can be seen as a strategic resource that is created through social networking processes (Dyer & Singh 1998) and provides an information channel through which firms learn about each other’s reliabilities and capabilities (Gulati & Gargiulo 1999).

In the venture capital context, Gompers et al. (2005) argue that entrepreneurs can build relational-specific assets with VC firms, and through their networks gain
exposure to potential suppliers, customers, and VCs. Their research argues that relational capital is replicable and that high-tech entrepreneurs can utilize the trust produced in the relationship to access information and knowledge to amplify other types of social capital such as cognitive and structural capital.

Often, the term “relational social capital” appears in scientific research to refer to the interpersonal connections developed during the social networking process (Granovetter 1992, Nahapiet & Ghoshal 1998). The boundary between relational capital and social capital is rather vague, and it is hard to differentiate one from the other. Through bibliographical analysis, Still et al. (2013) suggest relational capital and social capital are two separate but closely related areas, a suggestion supported by the fact that relational capital literature refers to social capital theory in its citations.

Relying on social capital theory, this dissertation pays special attention to the relational aspect of social capital. The rationale for further exploration of relational capital is that while two firms might agree to achieve the desired outcomes, the implementation of this agreement strongly depends on interactions between the individuals who represent their respective firms – in this case, INVs and VC firms. The impact of relational capital on a new business venture depends on all the actors who can create value for the organization. Without a historical track record, a new venture’s external relations rely heavily on the entrepreneur’s personal network, because a business network is not yet accessible (Hite 2005, Johannisson 1988, Johannisson et al. 2002). Creating relational rent is an important process to create value for the INV’s survival and growth through development of trust and active interactions (De Clercq & Sapienza 2001).

Relational capital is a multifaceted concept. Prior studies categorized it from different angles and in different contexts. In alliance studies, relational capital is a basis for knowledge transference through organizational learning that potentially prevents partners from engaging in opportunistic behaviors (Kale et al. 2000). Table 2 summarizes the prior research about relational capital dimensions from various organizational contexts.
Table 2. Summary of dimensions of relational capital

<table>
<thead>
<tr>
<th>Author/year</th>
<th>Dimensions</th>
<th>Context</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nahapiet &amp; Ghoshal (1998)</td>
<td>Trust, Norms</td>
<td>Social capital discussions</td>
</tr>
<tr>
<td>Kale et al. (2000)</td>
<td>Trust, Respect, Friendship</td>
<td>Alliances</td>
</tr>
<tr>
<td>Clercq &amp; Sapienza (2006)</td>
<td>Trust, Social interaction, Goal congruence</td>
<td>VCs and portfolio company performance</td>
</tr>
<tr>
<td>Weber &amp; Weber (2007)</td>
<td>Trust, Shared norms, Cognitive fit, Affective fit</td>
<td>Corporate venture capital and radical innovation</td>
</tr>
<tr>
<td>Blatt (2009)</td>
<td>Trust, Identification, Obligation</td>
<td>Entrepreneurial teams</td>
</tr>
<tr>
<td>Liu et al. (2010)</td>
<td>Trust, Transparency, Partner interaction</td>
<td>Knowledge acquisition in alliances</td>
</tr>
<tr>
<td>Duparc (2012)</td>
<td>Internal relations among employees, External relations with stakeholders</td>
<td>Innovation</td>
</tr>
</tbody>
</table>

Based on summaries of prior studies, the relational capital definition given in this study is the level of trust and transparency developed in the course of interactions between INVs and VC firms that leads to positive venture capital decisions and value creation for new venture internationalization. Trust here refers to good faith that develops over time between entrepreneur and venture capitalist, which leads to mutual understanding and avoidance of being misled in its interactions (Inkpen 2000, Robson et al. 2008, Welter 2012). Transparency here refers to a willingness to share and discuss market-, product-, and technology-related information, processes, and data to achieve goal congruence and solve problems collaboratively (De Clercq & Sapienza 2006, Hamel 1991, Inkpen 2000, Liu et al. 2010). A course of interaction includes all activities and events such as on-site visits, face-to-face discussions, and regular meetings that create relational capital or relational rent, or that generate goodwill for cooperation (Bresman et al. 1999, Subramaniam & Venkatraman 2001).
With the definition and context of relational capital now clear, the following subchapters will trace the venture capital investment process and discuss the key factors that might affect relational capital formation in the venture capital decision-making process. These subchapters also will discuss the outcomes of relational capital in post-investment activities.

3.3 Formation of relational capital in pursuit of venture capital for internationalization

This subchapter reviews and discusses the actions entrepreneurs take to raise venture capital, particularly for early internationalization. The prior studies on venture capital and venture internationalization focus mainly on post-investment activities (i.e., after the funding decision has been made) rather than pre-investment activities and decisions (Payne et al. 2009). To capture the entire picture of venture capital and new venture internationalization, this study starts with exploring entrepreneurial activities targeted at raising investment for new venture internationalization in the pre-investment stage.

Extant research has addressed the importance of networks and the outcomes related to survival and growth of new ventures (e.g., Coviello & Munro 1997, De Clercq & Arenius 2002, Gerpott & Jakopin 2005, Mudambi & Zahra 2007, Prashantham & Dhanaraj 2010, Sapienza et al. 2006). However, little research effort has been devoted to studying how entrepreneurs build and utilize relational capital while obtaining their first external financial support, which is considered one of the key components in the venture creation process (Reynolds & Miller 1992). In the venture capital funding context, general consensus holds that relational capital allows entrepreneurs to gain access to VCs (Liao & Welsch 2005), but the link to VCs through relational capital does not guarantee a positive funding decision for internationalization.

The internationalization outcomes of a new venture may potentially be achieved through relational capital (Agndal et al. 2008, Mort & Weerawardena 2006, Prashantham & Dhanaraj 2010, Zeng et al. 2009). The question of whether (and, if so, how) relational capital potentially contributes to the venture capital decision-making process remains unexplored within the context of an entrepreneur supporting successful foreign market operations. Research into relationship formation efficiency that affects the success and duration of the process of raising venture capital can be seen as supporting this line of reasoning (Hallen & Eisenhardt 2012). Although several studies (Alexy et al. 2011, De Clercq &
Sapienza 2006, Hallen & Eisenhardt 2012) point out the importance of relational capital in a VC firm’s decision-making process, how exactly it affects the funding decisions for INVs still demands systematic research. This subchapter explores how relational capital is built between the INV and VC firm and its importance to the ultimate signing of a venture capital agreement. The key factors affecting the formation of relational capital are defined by following each stage of the decision-making process.

### 3.3.1 In the origination phase

VCs discover potential deals through three channels: entrepreneurs, intermediaries, or referrals from their network during the deal’s origination phase (De Clercq et al. 2006). Entrepreneurs can proactively search for funding and directly approach VCs; however, unsolicited deals proffered by entrepreneurs are considered by VCs to be among the most risky cases unless the entrepreneur is referred to the venture capitalist by a network contact (De Clercq et al. 2006, De Clercq & Sapienza 2006). Deals generated by intermediaries are also a less favorable choice for VCs, because intermediaries expect a share of the profits and thereby lower the total earning potential of the deal (Lu & Hwang 2010). Thistoll and Pauleen (2010) indicate that VCs tend to limit their engagement with potential contacts, motivated by the need to protect their reputation through carefully choosing the entrepreneurs with whom they sign contracts. In short, VCs prefer to invest in ventures recommended by referrals from their networks.

Prior professional experience obtained through training and work not only contributes to what one knows, but also who one knows. Accordingly, a wise entrepreneur takes every opportunity to develop relational capital with the people he or she knows (Hsu 2007). In the early phases of new ventures, entrepreneurs only control a few resources. This “resource poverty” of the new venture drives entrepreneurs to actively engage in their existing networks to exchange ideas and tap into resource-providers’ networks. Once in the venture capital setting, entrepreneurs likewise tap into the VCs’ networks to access financial resources. A prior personal relationship between entrepreneurs and VCs also enhances further cooperative investment relationships (Timmons & Spinelli 1999).
3.3.2 In the screening phase

VC firms have specific criteria for the size of investments they will make and the industries and geographic locations in which they will do business (Fried & Hisrich 1994). Most proposals are rejected in the screening phase in order to minimize the usage of time. VCs usually know each other’s investment policies, preferences, and capabilities, leading to potential match and mitigation of investors’ social risks (Batjargal & Liu 2004). Many proposals that have passed the venture capital-specific screening might also be rejected without extensive review when the VCs do not have any pre-existing knowledge about such business plans (Bengtsson & Hsu 2010, Fried & Hisrich 1994).

Likewise, a new venture planning to internationalize might reject a venture capitalist if the venture capitalist lacks the knowledge and resources to support internationalization activities (George et al. 2005). Therefore, entrepreneurs may invest more attention and effort in pitching to VCs who specialize in the new venture’s industry and remove from consideration those who do not.

Interaction occurs and information flows between the entrepreneur and VCs during negotiations. However, information shared even during social occasions increases the entrepreneur’s understanding of the VCs’ investment policies, which helps the entrepreneur to tailor his or her pitch to the VCs’ particular interests. In the same way, VCs learn the capabilities of the entrepreneurial team, the business’s activities, and the key competitive advantages of the firm. All information exchanged during these interactions leads to the INV’s either passing or failing the screening process.

In other words, without communication and information exchange, “match” and “fit” cannot be achieved. Building of relational capital increases the frequency of this communication and information exchange. It can be concluded that the likelihood of a new venture passing the screening phase increases as the VCs learn more about the venture’s internationalization process, strategy, and network.

3.3.3 In the evaluation phase

Earlier research on venture capital has advanced our understanding of VC firms’ selection process prior to investment (MacMillan et al. 1986, Tyebjee & Bruno 1984). The literature on the venture selection process suggests that new venture proposals should meet investment selection criteria related to the top members of the venture’s management team (Baum & Silverman 2004, Patzelt 2010, Zarutksie

A key issue faced by VCs is whether to invest in typically more costly INVs or less risky domestic new ventures. The venture capital firm’s decision depends on how it assesses and leverages risk and return, especially since early internationalization may endanger the survival of the young firm (Sapienza et al. 2006). On the other hand, high growth may not guarantee high profitability (Lu & Beamish 2006). INVs pursuing early internationalization signal to VCs the potential for increased profits; and indeed, growth is the dominant incentive for VCs funding INVs. Due to internationalization-related risks, VCs may evaluate INVs more carefully prior to investment, searching for the best qualified ventures that fit the VC firm’s portfolio and from which they can subsequently exit successfully (LiPuma 2006). In the earlier established criteria of venture capital selection process shown in Table 1, assessment of relational capital of entrepreneur and controlling internationalization related risks are missing from the discussion, as the selection criteria has been developed based on the startups without early internationalization.

According to the evaluation criteria in Table 1, the investment decision depends on how capable the entrepreneur or management team is to mitigate liabilities and risks and reduce costs associated with the internationalization process. The internationalization process begins with obtaining relevant market information to identify foreign market opportunities. Finding relevant market-entry information depends heavily on the strength of the venture’s and management team’s business and social networks (Agndal et al. 2008, Zeng et al. 2009). With a strong network, entrepreneurs increase their access to information, resources, and knowledge, which affects the outcome of new ventures (Johanson & Vahlne 1977), enables the venture to reduce the high setup costs of internationalization associated with lack of international experience (Cooper & Dunkelberg 1986, Sapienza et al. 2006), and influences the venture’s appraisal of foreign market barriers (Santos-Álvarez & García-Merino 2010). The expertise of other firms and third parties in a relational network may help entrepreneurs avoid some of the risks of internationalization and improve the international performance of the firm (Agndal et al. 2008, Zeng et al. 2009).

Mort and Weerawardena (2006) indicate that international entrepreneurs should actively identify initial foreign market opportunities through their primary
networks and build up secondary networks to exploit those opportunities (Prashantham and Dhanaraj 2010). By utilizing the entrepreneurs’ relational capital in international markets, new ventures can gradually develop a routine for entering new markets and save time and costs related to developing internationalization capabilities (Sapienza et al. 2006).

Relational capital can help INVs obtain the critical resources needed for internationalization. The relationships established enable new ventures to overcome the liabilities of smallness, newness, and inexperience. When new ventures tap into foreign market networks through building and using relational capital with other firms, it is an effective means of increasing the chances of being funded – in addition to tackling the liabilities of foreignness and outsidership. Accompanied by improvements in network positions in foreign markets, new ventures gain market visibility, thus leading to greater chances of being acquired by industry buyers.

McDougall et al. (2003) argue that international new ventures exhibit more aggressive behavior than domestic new ventures, citing factors such as entrepreneurial team experience, strategy, and industry. These more aggressive ventures maximize their potential value by identifying strong international opportunities before making a strategic internationalization decision. In a related way, VCs interested in funding INVs have expectations for how the new ventures sell their products in the foreign target markets, with whom the ventures form alliances and partnerships, and what distribution channels the ventures choose (Proimos & Murray 2006).

Fundamental customer value creation involves innovation, production, and delivery of products to international markets in an effort to achieve competitive advantage and increased financial outcomes. However, value creation alone does not lead to financial performance, as firms must have the ability to appropriate value in order to turn the value into profit (Mizik & Jacobson 2003). Successful internationalization of new ventures depends on the ability of entrepreneurs to use relational capital and extract value from it, eventually appropriating that value to achieve international growth.

Mort and Weerawardena (2006) suggest international entrepreneurs should actively identify initial foreign market opportunities through their primary networks and build up secondary networks to exploit those opportunities. Prashantham and Dhanaraj (2010) empirically show how successful ventures extract value from these kinds of relationships through learning about international
markets and useful technologies and by leveraging ties from the company’s current network to acquire knowledge of the practices of other networks.

No single capability or activity determines a firm’s ability to appropriate the value created by innovative products or through process innovation (Mizik & Jacobson 2003). Relational capital is seen as an isolating mechanism to differentiate the firm from competitors and achieve advantage. Indeed, the internationalization of new ventures should be related to value appropriation from relational capital.

According to the summarized evaluation criteria, funding decisions also depend on the network relationships the new venture has in the foreign markets. New ventures usually engage in relationships with larger firms in an international network to develop their products. Involvement in these networks enables the new venture to achieve foreign market entry, and thus gradually increases market visibility. This increased visibility can make the new venture a candidate for acquisition by another firm within its network (Coviello & Munro 1997). In line with prior research (e.g., Coviello & Munro 1997), Kiederich and Kraus (2009) argue that internationalization of new technology-based firms may increase the chances of becoming acquired by networking. Acquisition potential is a clear benefit to a venture for, in practice, VCs are more willing to invest in new ventures that have already shown clear exit potential, either through IPO or acquisition. Thus, new ventures that improve their network positions by utilization of relational capital in international markets affect venture capital investment decisions.

To conclude, relational capital makes it possible for a new venture to identify foreign market opportunities, build networks, reduce setup costs, and increase market visibility, all of which accelerate internationalization and increase the likelihood of successful exit for the venture capitalist (Wennberg et al. 2010). Moreover, the entrepreneurs themselves may be more willing to accept the additional risks associated with internationalization when they find the international markets familiar (McDougall et al. 2003). The role relational capital plays in the deal evaluation process is to help entrepreneurs mitigate the liabilities of smallness, inexperience, newness, foreignness, and outsidership. With the decrease of internationalization costs and increase of international growth potential, new ventures become more attractive investment candidates for VCs. Controlling liabilities of INV internationalization is an important factor from the venture capital firm’s perspective in the due diligence process.
3.3.4 In the deal structuring phase

The creation and use of knowledge through relational capital as a part of a company’s strategy helps the company attain competitive advantage and enhances the firm’s value (Roos & Roos 1997). Given that relational capital involves trust, social interaction, and shared goals or norms (De Clercq & Sapienza 2006), building relational capital can partially reduce conflicts of interest and help the parties obtain the benefits potential to a relational exchange (Kale et al. 2000). VCs carefully design the contracts that assign control rights between themselves and entrepreneurs to mitigate any agency problems after a funding decision (Kaplan & Strömberg 2005). Alternatively, VCs might utilize relational capital as a mechanism for controlling the entrepreneur’s behavior in the future.

A venture capitalist’s network of relationships can offer a wide range of opportunities for and assistance in the internationalization process of new ventures. The venture capitalist’s network includes connections to service providers – e.g., deal flows, headhunters, patent lawyers, and investment bankers (Hochberg et al. 2007). Indeed, this existing relational capital may provide the needed links to key suppliers and customers (Busenitz et al. 2003) and also generate other investors for second round financing (Hochberg et al. 2007, Sapienza et al. 2006). In general, the performance of portfolio companies may be enhanced by the venture capitalist’s relational capital (De Clercq & Sapienza 2006). New ventures that need to leverage resources and capabilities from the network partners tend to stay committed after venture capital investment.

Yet the venture capital industry itself has only during the last decade started intensively to enter international markets and often lacks foreign investment experience and knowledge (Wright et al. 2005). Thus, the internationalization of portfolio new ventures complicates the situation due to the limited abilities of VCs to monitor distant operations (De Prijcker et al. 2012, LiPuma 2012). However, by building relational capital with VCs, entrepreneurs may imply their willingness to be monitored and controlled once the venture internationalizes, thus sending a signal of committed collaboration and decreased agency costs to the venture capitalist. From the entrepreneur’s viewpoint, in addition to funding, relational capital may offer new ventures better access to the valuable network of the venture capitalist.
3.4 The utilization of relational capital for internationalization in the post-investment phase

The last subchapter discussed how the entrepreneur can influence the venture capitalist’s decision-making process by actively forming relational capital. It clarified the role relational capital plays in each stage of the decision-making process and the importance of building relational capital to raise venture capital for early internationalization. Venture investment includes two stages: the pre-investment stage and post-investment stage. The next sections discuss the utilization of relational capital in value appropriation of venture capital, as well as the potential benefits venture capital may obtain in the post-investment stage.

The existing literature emphasizes the relationship between VC firms and the perceived internationalization performance of their portfolio firms, e.g., increase of export intensity, with value added and screening (Sapienza 1992) at firm level. Meanwhile, related studies have shown how VC firms often require involvement in strategic decision-making to ensure that the entrepreneur’s decisions are aligned with the VC firm’s expectations and stakeholders’ interests (Floyd & Lane 2000, Judge & Zeithaml 1992). To accomplish this involvement, VCs usually take seats on the board of the new venture as a means of influencing the entrepreneur’s decisions (Sapienza et al. 2000). Boards of VC-backed new ventures consist of both insiders (e.g., entrepreneur, managers) and outsiders (e.g., venture capital investors) who have significant ownership in the firm as well as the power and knowledge to impact the venture. VCs who are board members hold significant equity in the venture and are most likely to become involved in the decision-making process through offering strategic input, personal support, and business contact (Sapienza et al. 1996, Sapienza et al. 2000).

Given that VC firms use board membership and voting eligibility as a control mechanism to monitor the entrepreneur’s decision-making and behavior (Hillman et al. 2002), entrepreneurs must adapt their decision-making process. As the INV’s and entrepreneur’s performance influences VCs’ judgment, entrepreneurs will do well to take VCs’ expectations into consideration to help maintain the plausibility of the venture for the next round of financing (Zarutskie 2007).

To advance this discussion, in addition to board representation as a control mechanism, it is important to study the utilization of relational capital in post-investment activities to learn whether relational capital plays a role in developing the internationalization process. Further, if the answer is in the affirmative – that relational capital does have a role in internationalization – what is achieved by the
entrepreneur and venture capitalist? If the answer is in the negative, what are the results?

The next subchapter studies two main activities undertaken by VC firms: monitoring and value-added services in the post-investment stage. It also reviews the relevant literature on potential achievements or conflicts resulting from relational capital in the post-investment stage.

### 3.4.1 Monitoring

Following the venture capital investment process, the main contribution of the VC firm to portfolio companies are monitoring and value-added services in the post-investment stage. Because the entrepreneur and venture capitalist work together to develop international business for the new venture, the potential for opportunistic behavior on the part of one or the other party may arise. This phenomenon can be attributed to concepts known as moral hazard, adverse selection, and perceptual asymmetry (Kaplan & Strömberg 2003a, Kaplan & Strömberg 2003b, Yazdipour 2009) – in short, agency problems.

Relationships are subject to “relational risk” – in this current context, that the entrepreneur may not act upon the VC firm’s interests while managing the new venture and spending the VC firm’s capital. Given the dyad relationship of entrepreneur and venture capitalist, the relational risk is reciprocal. The VC firm’s decisions and guidance to the INV may not represent the best interests of the entrepreneur (Arthurs & Busenitz 2003).

For instance, the VC firm is a provider of capital and operational advice in addition to being in a position to search for market opportunities. In contrast, the entrepreneur who founded the high-technology new venture often has a strong technical background (Balkin & Swift 2006) and is enthusiastic about developing cutting-edge products and early-stage projects. The entrepreneur simply may lack the motivation and skill for developing an international, high-growth company. In this scenario, the entrepreneur’s and venture capitalist’s goals are not always perfectly aligned. The entrepreneur has an information advantage regarding scalability from a technology perspective. The venture capitalist, on the other hand, has better knowledge of management and marketing and the kind of financial know-how that facilitates successful commercialization of a new venture (Cable & Shane 1997, Koskinen et al. 2014). The resulting goal incongruence and information asymmetry can lead to the aforementioned agency problems of adverse selection or moral hazard (Sapienza & Gupta 1994).
The fact of the matter is that assessment of the entrepreneur’s goals and decisions requires significant cognitive effort on the part of the VC firm. In a typical case, from the contract perspective, the VC firm controls the INV through staged financing, setting up milestones with requirements for regular reporting to reduce risk. However, this contractual control mechanism increases the transaction costs for the VC firm.

In a worst-case scenario, VCs exercise control disproportionate to the size of their equity investment, sometimes replacing an entrepreneur/CEO by leveraging the power of its board representatives (Lerner 1995). Regardless of how defined or detailed a legal contract is, it cannot anticipate all potential problems that can arise between an INV and a VC firm, particularly in a highly uncertain international environment. Disagreement and conflict is to be expected in any INV/VC firm dyad (Higashide & Birley 2002, Parhankangas & Landström 2004).

From the social or institutional perspective, the process of building relational capital naturally leads to the revelation of information about the background and interests of the entrepreneur. Maxwell and Levesque (2014) argue that business angels consider a long-term relationship with the entrepreneur an important factor affecting investment decisions, because agency problems during post-investment activities can be reduced dramatically when a foundation of trust is enjoyed by the two actors.

Investigating the social nature of this dyadic relationship is important to gain a better understanding of a venture’s efficiency, productivity, and effectiveness (Higashide & Birley 2002). Viewing the relationship between an INV and VC firm in a holistic way can help identify situations in which the goals and interests of the venture capitalist and entrepreneur are aligned, so that both parties are committed to developing a trusting relationship.

When goals and interests are aligned, both parties are more willing to offer the information and knowledge (Cable and Shane 1997) that is needed to jointly develop the INV. Information contributed voluntarily by both parties enhances efficient decision-making within INVs. It not only reduces the amount of monitoring time allocated to the INV by the venture capitalist, but it also reduces INVs’ information reporting costs (Sapienza 2007). From the venture capitalist’s perspective, the question of whether relational capital can reduce agency problems in financing awaits the empirical evidence to be revealed in a later phase of this research.
3.4.2 Value-added services

Many researchers have studied value-added services, beyond financial capital, that VC firms bring to portfolio companies. The studies focus on the nature of the value that has been added to the new venture and how the value-added services improved the performance of portfolio firms. Research also has made progress in terms of understanding under what conditions a VC firm will contribute even more. In this study, the focus is on relational capital and its role in new venture internationalization. The special attention is paid to how these value-added services can be enhanced by relational capital between INVs and VC firms.

Network relationships of VC firms as a value-added service

INVs do not necessarily own many assets, but they do control vital assets through their network for international business development (McDougall 1996). New ventures rely on key formal relationships and strategic alliances to obtain resources required for internationalization. However, limited attention has been paid to the impact of the VC firm as a network partner for the internationalization of portfolio new ventures. This omission is significant, as VC firms are critical network resource providers for new ventures (e.g., Bygrave & Timmons 1992, Gompers & Lerner 2000).

The VC firm’s relationships include a network of service providers including recruiters, patent lawyers, and investment bankers (Hochberg et al. 2007). Such network resources can provide necessary links to key suppliers and customers (Busenitz et al. 2003) and also draw in other investors for second-round financing (Hochberg et al. 2007, Sapienza et al. 2006). Prior research points out that VC-backed new ventures receive knowledge, valuable resources (Fernhaber et al. 2009, Lu & Beamish 2001), professional training and strategic advice related to partnering opportunities (Sarkar et al. 2001). Using multiple case studies, Lutz and George (2012) show that VCs often recruit a CEO through the VC firm’s network and provide heterogeneous managerial knowledge and resources to assist in new venture internationalization.

Meanwhile, their study also implies that aspirations for growth in foreign markets on the part of the VC firm increases the aspiration level of entrepreneurs to involve themselves in international business, and ultimately increases the scale of internationalization for the new venture (Lutz & George 2012). Gulati (2007) reveals that the VC firm’s network position and its ability to access information
minimize the risk of unpredictable partner behavior. Therefore, information, knowledge, and network resources provided by VC firms reduce the liability of foreignness, which makes a new venture more capable of entering a foreign market.

By quantitative analysis of U.S.-based, VC-backed new ventures, Fernhaber and McDougall (2009) indicate that the knowledge and reputation resources of VCs positively influence the scale and scope of new venture internationalization. This suggests that venture capital may improve a new venture’s international performance by providing necessary knowledge to mitigate the liability of foreignness. Similarly, affiliation with a prominent VC firm helps a new venture access a better network position to obtain valuable resources (Hsu 2005, Ozmel et al. 2013, Stuart et al. 1999). This affiliation also helps the new venture overcome the liability of newness, as it signals to third parties the quality of the unknown venture based on the known quality of the VC firm (Large & Muegge 2008, Stuart et al. 1999).

Syndication as a control mechanism for venture capital investment has been found to increase export revenues and sales growth (Smolarski & Kut 2011). In terms of the value of new ventures forming alliances, syndication also provides complementary management skills and the shared social capital of the investors to the portfolio (Brander et al. 2002, Tian 2011). Lerner (1994) and Wang et al. (2012) as well as Ozmel (2013) suggest that syndication provides more access to additional resources and proclaim that the more networked a VC firm is, the more resources it is able to provide. VC firms are motivated to syndicate with other financiers because the implied “safety in numbers” mitigates the risks involved with the uncertainty of new ventures (Lockett & Wright 2001).

Venture capital and product innovation

Kortum and Lerner (2000) offer statistical evidence that suggests that the involvement of venture capital funding substantially increases the number of patented innovations. They assert that a dollar of venture capital spent appears to be worth about three times more in terms of stimulating patenting than a dollar spent on a corporation’s traditional research and development activities.

VC firms often invest in high-technology new ventures with innovative products. Due to the fast obsolescence of technology and limited resources, new ventures have to continuously develop products together with alliance and network partners, or even participate in larger projects with their competitors – so called “co-opetition” networks (Lechner et al. 2006). Otherwise, such projects would not
be attainable for startups. VC firms have both the motivation and the network resources to offer opportunities to form strategic alliances within their own portfolio firms (Chang 2004, Wang et al. 2012) – a wise move, as VC-backed ventures with more alliances tend to garner higher IPOs (Chang 2004, Wang et al. 2012).

Wang et al. (2012) state that VC-backed new ventures selectively choose partners with access to the resources most critical to building competitive advantage and reduce firm-specific environmental risk by leveraging the VC firm’s network. Based on a single case study, Strömsten and Waluszewski (2012) clarify the role of the VC firm in governance of resource interaction within networks. Their study indicates that venture capital involvement affects the development and sales of products, with whom the new venture interacts, strategic decisions related to the scope of the developing knowledge area, and the ability of the new venture to build relationships with portfolio suppliers and customers. Thus, VC firms not only offer inter-organizational cooperation opportunities (Hsu 2006, Lindsey 2008), but also lead the direction of formation of relationships between portfolio new ventures.
Fig. 4. A summary of utilization of relational capital

This subchapter concludes with Figure 4 that illustrates utilization of relational capital and the potential benefits and conflicts that result from development of relational capital.
3.5 Theoretical model: a priori model

To conclude the prior literature regarding the role of relational capital in the venture capital process discussed in the previous subchapters, a theoretical model – shown in Figure 5 – is proposed to describe the type and role of relational capital in an INV’s process of raising venture capital and interacting with a venture capital firm. As the literature indicates, relational capital can mean different things for the entrepreneur and the venture capitalist in each phase of venture capital decision-making and post-investment activities.

In the deal origination phase, relational capital is a referral mechanism for the entrepreneur that increases the INV’s chance of being formally referred to the venture capitalist by a trusted source close to the venture capitalist. For the venture capitalist, relational capital helps generate high-quality deal flows. The first construct included in the theoretical model is “appropriate referral,” which helps connect the entrepreneur and venture capitalist. Therefore, appropriate referral is considered an important factor affecting formation of relational capital.

In the deal screening phase, relational capital opens a communication channel between the venture capitalist and entrepreneur via active interactions. Interaction helps entrepreneurs understand the venture capitalist’s investment policies so that the entrepreneur can subsequently craft an appealing international strategy. As a venture capitalist’s evaluation is naturally biased toward investment opportunities that are based on decision-making processes similar to his own, the entrepreneur can take this opportunity to demonstrate logical alignment (Murnieks et al. 2011). The entrepreneur also can withdraw the proposal at this early stage of the pitch if a lack of fit between the INV and VC firm is perceived.

The deal screening phase also offers the venture capitalist the chance to obtain information about the INV’s internationalization strategy before committing. Chiang and Ko (2009) argue that internationalization increases costs for the VC firm. As such, additional information provided by the INV can effectively reduce the cost of capital (Botosan 2000). The theoretical model proposes that interaction equates to formation of relational capital for new venture internationalization.

In the deal evaluation phase, the primary concern for the venture capitalist is controlling internationalization-related liabilities, risks and investment costs. In this phase, relational capital is more important for the VC firms than for the INVs. Relational capital helps entrepreneurs prove that they are capable of successfully entering foreign markets and reducing the setup costs of internationalization. Increased foreign market visibility as proof-point is another element critical to a
positive funding decision (Hallen & Eisenhardt 2012) as relational capital is the mechanism for mitigating internationalization liabilities and risks. Similarly, the ability of the venture capitalist to control liabilities and costs associated with new venture internationalization affects the formation of relational capital in the deal evaluation phase. For that reason, the entrepreneur should demonstrate the ability to execute the internationalization plan presented to the VC firm. Controlling the INV’s liabilities and risks is one of the important factors influencing the formation of relational capital with the VC firm.

Valuation is the key issue to be negotiated in the deal structuring phase. Beyond the mere investment contract, relational capital can be used by the venture capitalist as a supplementary control mechanism to prevent opportunistic entrepreneurial behavior. Mutually developed relational capital may increase the willingness of the entrepreneur to voluntarily provide additional information, thereby reducing the cost of future investment. Although the entrepreneur always wants a higher value for the INV than that offered by the VC firm, the eventual agreement on valuation determines the formation of relational capital between the INV and VC firm in the theoretical model.

After the venture capital decision has been made in the INV’s favor, the VC firm’s activities progress to monitoring and value-added services. Now the mutually developed relational capital makes it possible for the entrepreneur to obtain further valuable network contacts from the venture capitalist to help facilitate ongoing investment rounds and internationalization.

Multiple benefits accrue as relational capital is utilized during the monitoring process. First, the VC firm learns more about the funded INV and the interests of the entrepreneur, which helps to ensure that future goals are aligned between the INV and VC firm. The second benefit is that the venture capitalist obtains information held by the entrepreneur, provided the relationship between entrepreneur and venture capitalist follows the procedural justice approach. Both of these benefits resulting from relational capital reduce the monitoring cost for the VC firm, which leads to the third benefit of utilization of relational capital with the entrepreneur.

Similarly, the entrepreneur is able to understand the goals and interests of the VC firm. Mutual understanding can reduce the potential for conflicts such as information asymmetry, moral hazard, and adverse selection, which are often assumed in agency theory. The model illustrated in Figure 5 suggests that utilization of relational capital can align the two parties. In turn, this alignment can derive additional value from relational capital.
In terms of value-added services, this model represents that with the development of relational capital, the venture capitalist is willing to contribute more than is customary: offering valuable contacts from within network relationships, management know-how, industry experience, and innovation acceleration. This concept aligns with venture capital research relating to how or under what conditions a venture capitalist contributes to the development of a new venture (Sapienza 1992).

Fig. 5. Theoretical model of relational capital formation and utilization between INV and VC firm
This theoretical model shown in Figure 5 illustrates the key factors that potentially influence the formation and utilization of relational capital in the venture capital process for new venture internationalization. The model addresses both the INV’s and VC firm’s interests in the formation and utilization of relational capital during the investment process.
“All genuine knowledge originates in direct experience, which is the basis of understanding objective things, and is the sole criterion for testing truth as well”

– Mao Zedong
4 Research design

Capturing the complexity of the relationship formation between INVs and VC firms requires a philosophical standpoint that facilitates understanding of such a relationship over time. As such, critical realism has become one of the most popular approaches to investigating business relationships and networks (Ryan et al. 2012). The present chapter covers the basic assumptions of this philosophy in relation to this study, devotes time to exploring why critical realism was chosen as the viewpoint for this study, and explains the manner of execution of empirical studies based on critical realism. The chapter also explores the case study design and describes the process of data collection, along with the effort made to ensure the data is fit for the purpose of the study. Finally, the chapter concludes with a discussion of data analysis strategies.

4.1 Research philosophy

Philosophical assumptions and beliefs in social science’s link to ontology, epistemology, and methodology are called a “paradigm” (Lincoln et al. 2011, Mertens 2010), and it is a paradigm which shapes the worldview of the researcher and guides the research behavior (Denzin & Lincoln 2009). This study adopts the worldview of critical realism as a research philosophy in relation to the basic assumptions about reality and knowledge. Critical realists believe that reality is independent of our knowledge of it, thus reality can never be fully understood due to hidden variables and a lack of ontological absolutes (Denzin & Lincoln 2009).

Critical realism has been widely applied to capture the complexity of business relationships and networks over time (Easton 2010, Morais 2011). The critical realism approach enables the researcher to critically investigate the conditions in which circumstances either stay the same or change over time, for the critical realist acknowledges the dynamic nature of business structures that are always changing based on continuous human agency (Easton 2002, Sayer 1992). The aim of critical realism is to investigate and explain what caused the events to happen (Dubois & Gibbert 2010). This standpoint is relevant to the INV/VC firm relationship, as this relationship is real and observable. Keeping such a relationship ongoing requires a series of events and activities that are driven by the entrepreneur’s and venture capitalist’s actions.

By adopting a position of critical realism, this study explores events and activities that influence the perceptions of entrepreneurs and VCs that lead them to
change their actions based on reactions to events in the relationship. In this way, this study is able to explore why INVs’ and VC firms’ relationships are as they are. Therefore, the critical realist understanding is a powerful means to explore causality within the INV/VC firm’s relationship formation and utilization in an organizational setting.

Ryan et al. (2012) developed a four-task Critical Realist Research Spiral as a guide for using the critical realist position. In the Ryan et al. model (2012), an abductive research design is the most suitable for collecting data when relying on critical realism as a philosophical standpoint. The theoretical lens guides the researcher to collect certain kinds of data, but without limiting collection to that kind of data alone. The abductive approach emphasizes the interplay between theory and the empirical data, contending that the theoretical framework constructs simultaneously and interactively with empirical observation (Dublos & Gibbert 2010).

In accord with Dublos and Gibbert (2010), Järvensivu and Törnroos (2010) point out that critical realism often adopts a research logic based on abduction, which requires a “back-and-forth” method of inquiry. Abductive reasoning focuses on a true dialogue between empirical and conceptual inquiry (Dublos & Gibbert 2010). Particularly for business relationship settings, the Ryan et al. (2012) model further suggests that the researcher should trace events leading to specification of causal mechanisms, as well as human actions, perceptions, and decisions, and the consequences of these on the relationship. The research at hand follows the abductive reasoning approach, emphasizing interplay between existing theory and the data, developing an *a priori* model from existing alternative theories, and developing an *a posteriori* model from the data collected via the Ryan et al. model (2012).

### 4.2 Case study design

The qualitative research method is used to uncover and understand unknown phenomena and action instances using rich and detailed descriptive data (Doz 2011, Ghauri 2004). The qualitative approach is important for international entrepreneurship research characterized by a “process” that requires close analysis (Davidsson & Honig 2003).

A case study is the research strategy suitable for a contemporary or ongoing phenomenon that cannot be separated from its real-life context (Tsoukas 1989, Yin 2003). Creswell (2013) defines case study as follows: “A qualitative research in
which the investigator explores a real-life, contemporary bounded system (a case) or multiple bounded systems (cases) over time, through detailed, in-depth data collection involving multiple sources of information, and reports a case description and case themes.” A case study can be regarded as the process of learning about a particular situation, and the case study itself is the product of that learning (Ghauri 2004). The choice of the case study method seeks to advance learning by understanding a specific problem rather than through generalization and to offer new insight into a theory and to build a new theory (Ghauri 2004).

The nature of the relationship between venture capital financing and early internationalization of a venture remains at the exploratory stage of research, thus it is especially suited to the exploratory nature of a case study investigation through interview data collection and archived data exploration. As the phenomenon under study is complex, a case study is the best approach to develop a model and understand the phenomenon in-depth.

A qualitative case study approach is applied in this research to uncover the specific details regarding how relational capital between an INV and VC firm is built and developed, and how it influences the obtaining of venture capital for internationalizing a new venture in a real-life context (Yin 2003). The case study method is particularly useful for exploring questions of “how,” relative to the operational links that need to be traced over time (Yin 2003). A case study addresses not only theory, but also offers an interesting real-life story to engage the reader. The interplay between theory and real-life cases helps prevent the problem of research becoming entirely self-referential and irrelevant (Siggelkow 2007).

There are two ways to accomplish a case study: single case study (e.g., Yin 2003) and multiple case studies (Eisenhardt 1989b). Debate in the management field is ongoing regarding which of these approaches is the most methodologically rigorous way to conduct a case study. The single case study method allows the reader to understand the context of the case in-depth, and a well-written story leads the reader to a deep understanding of a particular social setting and phenomenon under study (Dyer & Wilkins 1991).

Eisenhardt (1989b), in her article “Building Theories from Case Study Research,” argues that the most powerful means to creating theory is through multiple case studies. Her argument relies on the replication and extension nature of multiple case studies, and asserts that a complete theoretical picture can be generated through piecing together the complementary aspects of a phenomenon emphasized in each individual case. Methodological rigor is achieved by specification of research issues, sampling, and measurement of constructs and
controls (Eisenhardt 1989b, Eisenhardt 1991). Both single case and multiple case studies (Ravenswood 2011) have been widely applied to business studies.

This research uses the multiple case studies approach and follows Eisenhardt’s research procedures to conduct the field studies shown in Table 3. The phenomenon under study is how to turn relational capital into venture capital, and how relational capital is formed and utilized between the INV and VC firm for new venture internationalization. However, several types of circumstances are represented in these real-life cases: some of the INVs succeeded at raising venture capital through formation of relational capital, and others did not. Some of the INVs achieved successful exit by utilization of relational capital, while others did not. The multiple case studies approach allows within-case analysis and cross-case comparisons among individual cases to explore why these different outcomes occurred in a real-life context (Eisenhardt 1989b).

It should be noted that this research differs from the traditional multiple case studies approach described in Eisenhardt’s article. In this research, cases serve as a context through which data is collected. The individual entrepreneurs’ opinions collected through each case will be summarized together as a collective group perspective. Similarly, the individual VCs’ opinions will be summarized to represent a VCs’ group perspective. The comparison analysis of relational capital formation and utilization in the venture capital investment process is not done within-case; rather, the comparison is accomplished between entrepreneurs and VCs as two groups. This research allows cross-case analysis for understanding the relational situations, events, and activities that occurred in each case, as well as exploration of why relational capital in each case is different from the others.

Table 3. Eisenhardt’s process of building theories from case study research and steps in thesis

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<thead>
<tr>
<th>Step</th>
<th>Activity</th>
<th>Thesis</th>
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<tbody>
<tr>
<td>1. Getting started</td>
<td>Defining research question</td>
<td>Chapter 1</td>
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<td></td>
<td>Possibly a priori constructs</td>
<td>Chapters 2 and 3</td>
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<td>2. Selecting cases</td>
<td>Theoretical, not random, sampling</td>
<td>Chapter 4</td>
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<td>3. Crafting instruments and protocols</td>
<td>Multiple data collection methods</td>
<td>Chapter 4</td>
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<td>4. Entering the field</td>
<td>Field notes</td>
<td>Chapter 4</td>
</tr>
<tr>
<td>5. Analyzing data</td>
<td>Two groups’ analysis and cross-case analysis</td>
<td>Chapter 5</td>
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<tr>
<td>6. Shaping hypotheses</td>
<td>Iterative tabulation of evidence for each construct</td>
<td>Chapter 5</td>
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<tr>
<td>7. Enfolding literature</td>
<td>Comparison with similar and conflicting literature</td>
<td>Chapters 6 and 7</td>
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<td>8. Reaching closure</td>
<td>Theoretical saturation when possible</td>
<td>Chapters 6 and 7</td>
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</tbody>
</table>
The multiple case study method is not driven purely by inductive logic, unlike a grounded theory approach, which relies strictly on the data to generate new theories (Glaser & Strauss 1967). A case study requires development of research hypotheses based on a systematic theoretical review prior to data collection (Eisenhardt 1989b). In fact, the research hypotheses or models developed through systematic literature review guide the direction of the development of the research design.

Therefore, this study adopts critical realism as a philosophical standpoint to understanding the INV/venture capital relationship by applying abductive reasoning and multiple case studies as a method. This research began with identification of the research questions, followed by a comprehensive literature review on INVs, venture capital, and relational capital. A theoretical model was constructed as an *a priori* model for guiding empirical study. The following subchapters 4.3-4.4 introduce the data collection and analysis in detail.

### 4.3 Data collection

In this study, I used semi-structured, in-depth multiple case studies, as case studies can help the researcher investigate a phenomenon in depth to provide a rich description and understanding of a particular situation (Walsham 1995). Interview was the main strategy to collect qualitative data. This interview-based research strategy was chosen because of a lack of existing research exploring the relationship between VC firms and internationalization of new ventures (Carpenter *et al*. 2003, LiPuma 2006). Interview-based research is well suited for exploratory and theory-building studies, particularly when the population of possible respondents remains small, as it was in my cases in Finland (Daniels & Cannice 2004). By analyzing and appropriating qualitative data collected within the context of venture capital financing and international entrepreneurship, the role of relational capital in raising venture capital and in post-investment activities during INVs’ internationalization processes is conceptualized (Doz 2011).

I began by conducting a literature review related to the fields of internationalization and the liabilities of new ventures, venture capital investment, and international entrepreneurship. This broad literature review guided me toward identifying the working concepts for which I would collect case evidence. The literature review also helped me to familiarize myself with the related studies, which helped govern how I led the interview discussions with the respondents (Daniels & Cannice 2004, Eisenhardt 1989b, Yin 2003).
In tandem with the extensive literature review, the second step involved field work in a VC firm for the purpose of understanding the operations of the firm to lend a framework to structuring the in-depth interview themes. During a two-week working stay in the VC firm, I observed their daily administrative work and carried out several interviews with different people, e.g., the CEO, the financial manager, and the fund manager. I collected initial data about the process of setting up the venture capital fund, venture capital investment selection criteria and procedures, as well as the VCs’ role in professionalization of funded firms. Meanwhile, I had the chance to visit a number of invested firms and interviewed CEOs in the portfolio of the VC firm. This preliminary data collection provided me with an interesting topic regarding relational capital and its impact on raising venture capital and internationalizing new ventures. Combining a literature review and an analysis of primary data, I established the research questions for this dissertation. The theoretical model developed and the research questions determined the foci and boundaries within the selected samples for this study. The piles of initial data also helped me to design interview themes for both entrepreneurs and VCs. All of these activities enabled me to avoid research bias by relying on careful design of research techniques and the preparation of qualitative research-related, semi-structured interview themes regarding the relationship between venture capital and new venture internationalization.

I interviewed more companies – including both INVs and VC firms – than I ultimately selected during the research process. All interviews are transcribed onto paper, although some of them will not be included in this dissertation. Data not included in this study is nevertheless valuable for better understanding the research phenomenon, and it provides me with insights regarding the relational capital building, development, and utilization process. The excluded data was mainly collected during the early stage of this doctoral project, between 2010 and 2013, and served as a priori data for shaping the initial design of theory-building research (McCutcheon & Meredith 1993). Table 4 depicts complementary data that was not included in the final analysis and its role in the research process.
Table 4. Complementary data in this study

<table>
<thead>
<tr>
<th>Time</th>
<th>Type of data</th>
<th>Role in research process</th>
</tr>
</thead>
<tbody>
<tr>
<td>June 2010</td>
<td>Participation in multiple workshops for a project about establishing a venture capital fund in Oulu, carried out by Center of Internet Excellence, University of Oulu</td>
<td>Formulating an interesting research topic for this study.</td>
</tr>
<tr>
<td>June 2010</td>
<td>Participation in negotiating with different stakeholders in Oulu Region</td>
<td>Understanding the research topic from different viewpoints</td>
</tr>
<tr>
<td>July 2010</td>
<td>Two weeks’ stay in an Italian VC firm – observation of daily operations, fund documentation</td>
<td>Having a better understanding of functionalities of a VC firm</td>
</tr>
<tr>
<td>July 2010</td>
<td>Two hours’ participation in a board meeting in an Italian venture capital-backed INV</td>
<td>Basic understanding of board meeting involving VCs and entrepreneur. Understanding how the joint decision was made.</td>
</tr>
<tr>
<td>July 2010</td>
<td>Four interviews with venture capital-backed entrepreneurs in Italy. Each lasted about 60-90 minutes</td>
<td>Understanding the importance of obtaining venture capital and development of entrepreneurial ventures</td>
</tr>
<tr>
<td>July 2010</td>
<td>Interviewing employee working in the VC firm</td>
<td>The roles of different staff played in VC firms. Obtaining information on investment examples and stories</td>
</tr>
<tr>
<td>July 2010</td>
<td>Interviewing two VCs and an angel investor in Italy</td>
<td>Creating knowledge of venture capital investment, investment policy, criteria and importance of relationship development</td>
</tr>
<tr>
<td>August 2010</td>
<td>Participation in discussions with Sitra, a Finnish angel investors’ network</td>
<td>Understanding gathering a group of wealthy investors and generating a good deal flow</td>
</tr>
<tr>
<td>August 2010</td>
<td>Participation in negotiating with other governmental venture capital funds</td>
<td>Having idea how governmental funding was initialized and worked</td>
</tr>
<tr>
<td>September 2010</td>
<td>Presentations and reports on progress of project of establishing a venture capital fund</td>
<td>Giving information to public audiences and stakeholders in the area</td>
</tr>
<tr>
<td>September 2010</td>
<td>Participation of event “Money talks”</td>
<td>Knowing current trends in Oulu, Finland</td>
</tr>
<tr>
<td>September 2012</td>
<td>As an observer in a startup training workshop, small talk with participating entrepreneurs and invited representatives of incubators and investors</td>
<td>Understanding the importance of training program organized for new ventures which search for venture capital</td>
</tr>
<tr>
<td>January 2013</td>
<td>Interviews with entrepreneurs who gave up approaching venture capital</td>
<td>Getting ideas why entrepreneurs would not like to choose venture capital as a financial resource channel</td>
</tr>
</tbody>
</table>

Complementary data collection was accomplished mainly through participant observation, observation, and interviews. Participant observation and observation
provided a detailed assessment of interpersonal activities and a first-hand account of events and context (Johnston et al. 1999). Through observation, complementary data offered me a deep understanding of the relationship between INVs, VC firms, and third parties, and helped me with drafting the interview questions. Since the complementary data had provided me with a solid basis for understanding the phenomenon around context of VC firms and INVs, it allows me to focus directly on the research topic, gather needed data and gain better understanding of perceived causal inferences.

With careful consideration of the quality of available data, out of all companies interviewed, I decided to include five venture capital-backed INVs as cases to describe the relational capital formation and utilization process in a clearer way and to facilitate in-depth analysis. The choice was made because qualitative sampling tends to be purposely selective rather than random (Miles & Huberman 1994). The first step was to set up theoretical sampling parameters in order to limit the number of cases fitting the pre-drafted research purpose and question of this study. In this study, the possible choices of the case companies are described in Table 5:

<table>
<thead>
<tr>
<th>Sampling parameters</th>
<th>Possible choices</th>
</tr>
</thead>
<tbody>
<tr>
<td>Settings</td>
<td>INVs, industry, location, type of VC investment, age of the company</td>
</tr>
<tr>
<td>Actors</td>
<td>Entrepreneurs, VCs, advisors, educators</td>
</tr>
<tr>
<td>Events</td>
<td>Networking events, financial talks, incubating events, pitching events</td>
</tr>
<tr>
<td>Processes</td>
<td>Getting in touch with VC, in process of raising VC, e.g., personal activities, public activities, entrepreneur firm-VC firm interactions, formal VC negotiations in process of working with VC, and the consequences after VC, e.g., board meetings, joint decisions</td>
</tr>
</tbody>
</table>

I started by determining the settings of the case companies. This study aims to investigate INVs, so all the cases should internationalize within six years of establishment. Typically, VC firms are interested in high-technological growth firms. Due to the sensitivity of entrepreneur-VC relationships, it would be hard to persuade informants to participate in interviews without trust. Therefore, Oulu is defined as a region for generating the potential case companies through my personal networks and with the help of my supervisors. Oulu is famous for ICT innovation and has many startups in the ICT industry. Private venture capital is the primary choice for this study, but in the Finnish system, public-private VC firms are possible and so can also be included for selection as cases. For the potential case companies, they may have received several rounds of venture capital.
investment. If this is the case, corporate venture capital may also be involved. In order to capture how INVs have developed early in their internationalization processes, along with how they have built up and utilized relational capital with their financial resource-provider VC firms, older ventures that have been backed by VCs can be the ideal choice to capture relational capital that evolves over time. There is no age limit if a firm met the criteria of having internationalized within six years of inception and having involved venture capital during the internationalization process.

The actors for interviews include entrepreneurs or key staff involved in building and utilizing relational capital with VC firms. For technological ICT startups, there would not be many employees at the early stage of the company. Often, one or two entrepreneurs act as CEO and are involved in building and utilizing relational capital with VCs. In this situation, the limitation for the study is the availability of the number of informants within a company. If the company is nursed by an incubator or public organization, the advisor can also be included for additional information about how the company has built and utilized VC, so as to avoid personal bias from a single informant. This study attempts to generate the whole picture, from both the entrepreneurs’ and VCs’ perspectives, and since VCs are active during the processes of building and utilizing relational capital, they are relevant interview subjects.

After identifying the case choices for this study, a list of possible companies that can serve as cases for my study is created. The second step was to make a strategic choice among those companies. To maximize the use of small samples in a multiple case study, researchers purposefully select cases based on maximum variation to obtain information on the significance of various circumstances (Denzin & Lincoln 2010). The “polar type” of sampling approach is adopted to keep the research sample extreme in order to better identify the factors that influence relational capital formation and illustrate the importance of relational capital and its utilization in raising and working with venture capital.

From the perspective of theoretical sampling, retrospective and real-time cases can mitigate bias toward retrospective sense-making and impression management (Eisenhardt & Graebner 2007). I decided to include both retrospective cases and real-time cases. The retrospective cases offer depth of analysis and rich data on the entire process of relational capital building and utilization, as well as the consequences of relational capital between INVs and VC firms on the destiny of the company. The real-time cases allow me to track relational capital as it developed.
between INVs and VC firms, and to make observations and accumulate longitudinal data on the relational capital process between INVs and VC firms. 

Finally, in this study context, five cases were carefully selected to represent different situations. All case companies are in high-technology industries. Due to the nature of the products, these companies often require internationalization very soon after inception. The case companies that are included in the research data are located in the City of Oulu, where the research project was carried out. The nearby locations of the case companies allowed me to build a close relationship with interviewees and to collect follow-up data whenever needed. As the relationship development process is rather sensitive, and because conflict-related issues may arise during the research, I decided to anonymize interviewees and their company information to avoid potential problems and maintain an ethical manner of research. The code names are given to five case companies in the thesis: *Chaining*, *Sending*, *Placing*, *Viewing*, and *Basing*. These code names represent the product characteristics of each company, but they also maintain the anonymity of both interviewees and companies, as was promised to the interviewees.

Case one – *Chaining*: represents the thoughts of entrepreneurs who ultimately abandoned venture capital as a financing option in the evaluation stage, due to the company’s reluctance to deal with relationship matters involving the VCs. However, *Chaining* still manages growth by other means of financing, and it remains in business at the present time. Despite its lack of venture capital financing, *Chaining* is a promising venture. Its failure to raise venture capital was not based on product issues, but on the failure of the relationship with the VCs. *Chaining* represents entrepreneurs’ thoughts regarding why sometimes relational capital is not able to be formed, developed, and utilized between entrepreneur and VC firm.

Cases two and three – *Sending* and *Placing*: these companies have successfully raised venture capital and continue post-investment activities with VC firms at the present time. These cases offer fresh experiences regarding the developing of relational capital and working with VC firms.

Case four – *Viewing*: this also is an older venture, one that successfully raised three rounds of venture capital before exit. The venture also achieved exit by merging with a U.S. company. The merged company then was bought by a large famous multinational company, and it continues as an active business entity. This case tells a complete story of relational capital with VC firms, both through upturns and downtowns in the relationship.

Case five – *Basing*: this venture was established in 2002 and successfully raised venture capital for developing the U.S. market in 2006. However, during the
post-investment stage, relational capital faltered, resulting in the venture’s failure. This case involving failure of the venture provides an opportunity to demonstrate what can go wrong with a VC firm so that companies can know what to be aware of in the future.

Fig. 6. Positioning case companies into successful and unsuccessful categories in pre-investment and post-investment phases

After carefully selecting the cases, the interviews were carried out mainly during 2012 through 2015. I persuaded the potential informants to participate in this research, focusing on enlisting respondents from both the entrepreneur and venture capitalist sides. As a researcher, I tried to create a favorable interview or research environment and establish a cordial relationship with interviewees in the case-study companies to derive reliable in-depth data. Primary data was collected mainly by interviews. I interviewed founders of five companies and, if accessible, I also interviewed their lead VC investors to draw a complete picture from both the entrepreneur’s and investor’s perspectives on the role of relational capital. The key informants for this study are described below.

The founder of Chaining, who also serves as CEO, was invited to interview. Primary data was mainly collected through interviews and partially collected through exchange of emails and comments from the interviewee in 2012 and 2013. All of the interviews, emails, and conversations were transcribed immediately after they were conducted and were analyzed at a later stage. Public information on
Chaining from the Internet, from the news, and from other sources was used as secondary data.

The founder of Sending was invited to interview as he had witnessed the entire funding process of Sending and served as CEO. The investor from Sending’s VC firm A also was interviewed to describe the investment process and relationship development with Sending from the venture capitalist perspective. Primary data was mainly collected through face-to-face interviews with the founder and the venture capitalist. All of the interviews were digitally recorded and transcribed into text immediately after they were conducted, then analyzed at a later stage. Public information regarding Sending from the Internet, from the news, and from other sources was used as secondary data.

The founder of Placing was invited to interview as he had witnessed the entire funding process of Placing; he serves as CEO of the company. The U.S.-based investors were also interviewed. They described the investment process and relationship development with Placing from the venture capitalist perspective. An American advisor based on Oulu who works for a public organization for startups was also interviewed in autumn 2015, as she had worked with Placing for the initial three years to develop U.S. markets and helped to attract U.S.-based investors. She had a good relationship with U.S. investors and was able to access internal business information, yet she maintains an outsider’s viewpoint. The primary data was mainly collected through face-to-face interviews with the founders and Skype-based calls with the VCs (who were located too great a distance away to interview in person) in 2013. All of the interviews and Skype calls were digitally recorded, transcribed into text immediately thereafter, and analyzed at a later stage. Public information regarding Placing from the Internet, from the news, and from other sources was used as secondary data.

The first key employee of Viewing, who served as CFO, was interviewed; he was not an original shareholder, but became one in a slightly later phase. He was a key player involved in the fundraising for Viewing and witnessed the entire process through exit. The primary data was collected through face-to-face interviews in summer 2015. All interviews with him were digitally recorded, transcribed into text immediately after they were conducted, and analyzed at a later stage. Public information and other documents collected from the interviewee became the secondary data of the case.

The founder of Basing, who serves as CEO and who witnessed the entire funding process, was invited to interview. He is a key negotiator and relationship-builder with VCs. Some of the data related to Basing had already been collected,
in 2011, and follow-up collection took place in 2013 and 2015. The primary data was mainly collected through face-to-face interviews with the founder. All interviews with him were digitally recorded, transcribed into text immediately after they were conducted, and analyzed at a later stage. Internet-based dialog through social media channels was also documented and transcribed. Public information on Basing on the Internet, in the news, and from other sources was used as secondary data. In particular, the master’s thesis written by Basing’s founder describing his feelings on the relationship with VCs was used as secondary data. By comparing his interviews and his description of the development of the relationship with VC firms, the quality and accuracy of the information was ensured.

### 4.4 Data analysis

The theoretical model and data collected from these five Finnish case INVs offer the basis for conducting data analysis. The purpose of analyzing qualitative textual data is to arrive at common themes (Lichtman 2013). The data analysis process involves a logical means of data organizing, categorizing, sorting, and shifting, as well as modeling from and interpreting the data (Ghauri 2004, Lichtman 2013, Patton 2005). I followed three main steps called the “three Cs: from coding to categorizing to concepts” as described by Lichtman (2013) to identify central themes for this study. 1) Coding: is a process of developing and refining interpretations of the collected data. There are two types of coding strategies; that are: codes are guided and determined by a priori, or, codes emerge from the data through a thoughtful reading of the transcribed material. 2) Categorizing: The transcribed textual data from an interview is gradually dissected into codes that will be organized into manageable levels of categories and subcategories. 3) Concepts: The final process involves identifying central concepts or themes that reflect the meaning of the data collected.

As described in the data collection section, I started with field work to identify research questions and gain understanding of the key concepts under study. Then, I began to collect data from the five case INVs. Data was mainly gathered via interviews, although multiple sources of data were taken into account, such as emails, publicly-available news and presentations, as well as a master’s thesis involving Basing, in which the founder described the feelings he perceived from VCs. The data collection process was long, lasting three years from initial interview to the last interview. Because data collection and analysis are interactive processes (McMillan & Schumacher 2014), data analysis could be started as soon as the data
was collected (Miles & Huberman 1994). It was not necessary to wait until after all interviews were conducted to start data analysis. Taking the advice of Miles et al. (2014) who suggest that data should be transcribed as soon as possible, I began with the first interview, transcribed it into text, and analyzed it immediately after transcription. Following this method, I began data analysis after completing the first interview, checked whether additional information should be sought in the following interviews, and started the next interviews. I focused on the interplay between gathering data, analyzing data, and asking questions (Lichtman 2013). Once all interviews were completed, I had already become rather familiar with my data (Creswell 2013, Esterberg 2002) through initial interpretation of each case.

For each interview, I transcribed the digitally recorded interview and field notes into textual language saved in a Microsoft Word document. All interviews were conducted in English, but none of the interviewees’ spoke English as their mother tongue, except for the advisor and the venture capitalist of Placing from the U.S.. Linguistic mistakes may be introduced when talking in a foreign language. The interviewees were able to present their thoughts and opinions in easily understandable English during the interviews, however. In order to be “true to the sources,” I decided when transcribing their statements for direct quotations in Chapter 5 (data analysis) to use their English as it was recorded on the digital recorder. I read each transcript thoroughly, proceeding line by line in order to familiarize myself with the raw data (Creswell 2013).

The first step for making sense of the data was to develop codes. Codes are “labels that assign symbolic meaning to the descriptive or inferential information compiled during a study” (Miles et al. 2014: 71). I used abductive logic and decided to use an *a priori* strategy for coding, which relied on a theoretical model developed based on literature, theory, and exploratory interviews in the field for determining codes. Keeping critical realism in mind as the philosophical standpoint for this study, I focused on the interplay between the theoretical model and the empirical data. Initially, coding was based on the theoretical model developed in Chapter 3. However, the empirical data showed information that had not yet been covered by the theoretical model and which might be meaningful for understanding relational capital formation and utilization between INVs and VC firms. I therefore coded and gathered the information as a list called codes that emerged from the empirical data. These emerging codes may enhance my understanding and interpretation of relational capital for further data analysis and may make a further contribution to literature.
During the coding process, I used the computer software QSR Nvivo (version 10) to facilitate data analysis of the vast amounts of raw material. Initially, the codes focused on INVs, venture capital, and relational capital, because the abductive research process identified these as the main themes under scrutiny. When more interviews were completed, new codes were identified and created until the last interview codes were completed. Five companies’ names were inserted into the Nvivo, labeled Chaining, Sending, Placing, Viewing, and Basing. The program helped to sort the data according to interviewees and to trace who had said what in relation to the codes; it also facilitated identification of the consequences of relational capital formation in the post-investment stage. With the help of Nvivo, the data was visualized by various codes. Once coding for all interviews had been done, all the codes were revisited, combined, and reduced into categories or moved into different categories. The categories were refined several times by removing redundancies and identifying critical elements.

Given the limitation of the empirical data that not all VCs from the five case companies had been interviewed, a case-by-case comparison was not suitable for this study. The cases served as contexts in which entrepreneurs’ and VCs’ data was collected. The data collected from the cases made it possible to make comparisons between entrepreneurs and VCs as two groups. I decided to combine the theoretical and emerging codes into categories for entrepreneurs and VCs for comparison, and I organized codes into categories according to pre-investment stage, focusing on relational capital formation between INVs and VC firms (Appendix 1), and post-investment stage, focusing on relational capital utilization between INVs and VC firms (Appendix 2). Each entrepreneur perceived relational capital differently, so, after the VC investment decision was made, the perceived relational capital and emotional feelings were coded and categorized under “relational atmosphere after VC investment decision” (Appendix 3). Furthermore, each construct and possible influence of relational capital formation on utilization was explored and investigated, such as the impact of the valuation of the firm and its possible consequences for relational capital utilization in the post-investment stage. After preliminary categorizations had been conducted on the basis of the model and empirical data, the categorizations were further organized into INV-related factors, behavioral factors, and VC firm–related factors that had effects on relational capital formation, the outcomes of relational capital utilization (summarized as tangible and intangible resources), and the possible consequences of relational failure in the post-investment stage.
The categorizing process enhanced my understanding of the different perceptions of entrepreneurs and VCs, as well as their motivations and expectations of relational capital formation and utilization. By jumping back and forth between theory and codes, categories developed. To answer the research questions, I ultimately chose to retain as central themes “factors affecting relational capital formation,” “INV/VC firm relational atmosphere” (that is, the link between relational capital formation and utilization), and “outcomes of relational capital formation and utilization.”

I continued the data analysis by exploring the interrelationships between relational capital formation, relational atmosphere, and relational capital utilization, aiming to explore how and why the relational atmosphere perceived during the relational capital formation process affected the utilization of relational capital in the post-investment stage between the INVs and VC firms. In the data analysis section, I described the role of relational capital in raising and utilizing venture capital with a cross-case comparison (Ghauri 2004: 118–120) from the entrepreneur’s perspective. Patton (2002: 440) argued that describing individual cases via cross-case analysis causes confusion. Therefore, relational capital formation and utilization was described on a case-by-case basis, based on the entrepreneurs’ description, to make each individual case clear. Given the limitation that fewer VCs from case INVs participated in interviews for this study, the VC’s perspective was not described in the same way as that of the entrepreneurs, that is, through a case-by-case analysis. Instead, the empirical data showed that the opinions of the VCs who were interviewed toward INVs were rather similar, so I decided to still present the VCs’ viewpoint in this study collectively in order to generate an overall picture of relational capital formation and utilization from the perspectives of both INVs and VC firms. The analysis of VC firms’ view was based on two VCs from two of the case studies and two other VCs from VC firms that had not invested in case companies. Once that had been done, I summarized entrepreneurs’ perspectives together and compared them with VCs’ perspectives on the topic. The central themes were analyzed across the cases, taking into account both entrepreneurs’ and VCs’ viewpoints.

To conclude the analysis by modeling and interpreting, I constructed an empirical model for illustrating relational capital formation and utilization between INVs and VC firms for new venture internationalization. The empirical model was compared with the theoretical model (Ghauri 2004), and finally the study was concluded with a conceptual model to illustrate my research contribution to literature.
“No practice, no gain in one’s wit”

– Luyou
Empirical analysis of relational capital formation and utilization

This chapter is the core of the dissertation and tells an intriguing empirical story. It begins with an introduction to the background of the selected cases and key informants and explains the rationale for why these cases are representative for this study. Then, it continues through the data that was collected from interviews with representatives of the case companies. The findings are divided into two groups: entrepreneurs’ and VCs’ perspectives. First, the thoughts and opinions of entrepreneurs and their understanding of relational capital with VC firms is summarized, coded, and compared. The second step analyzes the data collected from VCs in a similar way. Last but not least, the perspectives of the two groups are further compared, analyzed, and discussed to answer the research questions and draw conclusions. The main purpose of this chapter is to shed light on understanding the importance of relational capital within the venture capital investment process between INVs and VC firms. Both positive and negative opinions from entrepreneurs and VCs toward relational capital formation, development, and utilization are considered and analyzed. By analyzing data from both the entrepreneurs’ and VCs’ viewpoints, the empirical understanding of relational capital in the venture capital process is described and deepened.

The backgrounds of the cases

This subchapter introduces the background of each case and the amount of funding raised from VC firms. Rounds of financing, number of investors, and other financial investment alternatives involved are also described. This subchapter ends with a summary and comparison of the cases.

Chaining builds, maintains, and designs electronic solutions for safety. (This general description of the products is used to avoid identification of the case.). Only Chaining does not refer to an amount of venture capital investment raised. Chaining has received government funding from Tekes as well as governmental venture capital investment in 2008. Chaining’s entrepreneur tried to raise private venture capital during the time period 2008 through 2012, but was not successful. Chaining manages to survive and grow through generating revenue, and is still active in the global market today.

Sending has successfully raised approximately 2 million Euros from two VC firms. Sending develops wireless telecommunication systems that provide
telecommunication services anywhere in the world, especially in remote areas. The company was founded in 2011 as a university spin-off. Sending received a venture capital investment in August 2014 aimed at commercialization of their technology and sales expansion into the international market. This round of investment amounted to approximately 2 million Euros. There are two lead investors as well as some private angel investors. According to Sending’s VC firm A, which focuses on investing in North Finland high-tech startups, Sending is thus far the largest investment they have made. Sending’s VC firm B is located in Finland but focuses on investing both domestic and overseas.

Placing has successfully raised over 9 million Euros (converted from U.S. dollars to Euros for readability in this study) from three investors, including governmental funding, venture capital, and corporate VC firms. Placing was founded in 2012 as a university spin-off. It provides solutions for positioning. Their technological solution is unique in that no external infrastructures are needed. Placing has attracted many investors from the Finnish government as well as U.S. venture capital and Asian corporate venture capital investments. Placing established a sales subsidiary in the U.S. in 2013, a year after their inception. Their R&D centers are located in Oulu and Helsinki, Finland. The team comprises researchers, computer scientists, software engineers, and market developers. The size of the team in total was about 25 persons at the time the interview was conducted. Placing has successfully raised about $5 million from Finnish and U.S. VC firms. The purpose of this investment was for launching Placing’s product and building its operation in the U.S. market. An Asian corporation invested another $10 million. Other public investors that finance innovation and early-stage technology ventures in Finland also invested in Placing.

Viewing was established to provide applications solutions for wireless devices. The company has raised three rounds of VC investment from multiple investors. In the third round, Viewing received over 1 million Euros from two VC firms. Viewing achieved exit via merger by a foreign applications solutions company for hardware business in 2008. A multinational company then purchased the merged company in 2012.

Basing obtained seed capital and successfully raised venture capital, internationalizing to the U.S. shortly after inception. The company, a provider of a platform for building applications, was a spin-off from an established company located in Oulu, Finland. Founded in 2004, Basing was the second venture founded by the entrepreneur, who also serves as CEO of the venture. In 2005, Basing started its internationalization process with particular focus on the U.S. market, more
specifically Silicon Valley in the U.S. The founder was invited to interview as he had witnessed the entire funding process of Basing. He initially obtained several million Euros as seed financing from Sitra and other private angel investors in 2005, followed by 3 million Euros venture capital investment from Basing’s VC firm A as lead investor. In addition, Basing raised funding from Finnish Industry Investment and Finnvera in summer 2006. With this investment, a new office was opened in Silicon Valley in 2006. Basing’s VC firm A is a leading early-stage technology VC firm investing in Finland, Sweden, and the Baltics.

Table 6. Interview and interviewee details

<table>
<thead>
<tr>
<th></th>
<th>Chaining</th>
<th>Sending</th>
<th>Placing</th>
<th>Viewing</th>
<th>Basing</th>
</tr>
</thead>
<tbody>
<tr>
<td>Year of establishment</td>
<td>2004</td>
<td>2012</td>
<td>2012</td>
<td>2002</td>
<td>2004</td>
</tr>
<tr>
<td>Year of internationalization</td>
<td>2006</td>
<td>2012</td>
<td>2013</td>
<td>2002</td>
<td>2005</td>
</tr>
<tr>
<td>Year of receiving VC</td>
<td>Not received</td>
<td>2014</td>
<td>2014</td>
<td>2004</td>
<td>2006</td>
</tr>
<tr>
<td>Amount VC received</td>
<td>No</td>
<td>2 million Euros</td>
<td>13 million Euros</td>
<td>10 million Euros</td>
<td>3 million Euros</td>
</tr>
<tr>
<td>Rounds of investment</td>
<td>No</td>
<td>1 round</td>
<td>3 rounds</td>
<td>3 rounds</td>
<td>1 round</td>
</tr>
<tr>
<td>Foreign VC</td>
<td>No</td>
<td>No</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Other funding received</td>
<td>10 Angels</td>
<td>Angels</td>
<td>Government</td>
<td>Angel</td>
<td>Government</td>
</tr>
<tr>
<td>Public VC</td>
<td>Government funding</td>
<td>Government funding</td>
<td>Government funding</td>
<td>Government funding</td>
<td></td>
</tr>
<tr>
<td>Venture exit</td>
<td>Not-related</td>
<td>Ongoing</td>
<td>Ongoing</td>
<td>Yes, acquisition</td>
<td>Yes, close up</td>
</tr>
<tr>
<td>Operational area</td>
<td>Digital solution</td>
<td>Wireless</td>
<td>Wireless</td>
<td>Wireless video</td>
<td>Internet</td>
</tr>
<tr>
<td>Length of interview</td>
<td>52 mins with the founder in 2013</td>
<td>55 mins with VC investor in 2014</td>
<td>60 mins with the founder in 2015</td>
<td>60 mins with founder in 2012</td>
<td></td>
</tr>
<tr>
<td></td>
<td>50 mins with Venture capital investor in 2015</td>
<td>45 mins with advisor in 2015</td>
<td>Follow-up 35 mins with founder in 2015</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>55 mins with founder in 2015</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Table 6 summarizes the key facts about the INVs interviewed for this research. Information on the INVs includes the years of establishment and internationalization, the year venture capital was received, the amount raised and
number of rounds of investment, as well as other funding sources and the industry in which the company operates. The details regarding timing and duration of interviews are also included.

5.2 Capturing the formation and utilization of relational capital in individual cases

This subchapter presents empirical data on the importance of relational capital for raising and utilizing venture capital within the venture capital investment process. Occurrences related to either accelerating or hindering the building and utilizing of relational capital are further described from both entrepreneurs’ and VCs’ perspectives.

The entrepreneur’s understanding of perceived relational capital with VC firms will be presented case-by-case. As not all of the VCs for each of the five case companies were accessible for interviews, it is not possible to describe their perception of relational capital on a case-by-case basis. Therefore, the VCs’ opinions are summarized together and presented by following the investment process starting at the point of the INV’s raising venture capital until the point of exit, provided the case company has reached exit. The VCs’ collective understanding of relational capital for investing in INVs will serve as supplementary commentary.

5.2.1 Individual INVs’ case studies described by entrepreneurs

The empirical data shows that the entrepreneurs of case companies may not yet be fully aware of the venture capital process before presenting investment proposals to VC firms. Most simply followed the ordinary steps for entrepreneurial business and started with a networking process in their local communities. Some first targeted wealthy individuals known as angel investors for seed phase financing, as well as governmental funding support for product development, commercialization, or internationalization. Later on, the companies might have been exposed to venture capital financing as an opportunity, at which point they started working with VC firms. What each company did to approach venture capital might not exactly follow each stage of the venture capital investment process as defined by the literature, but the process would be rather similar.

The initial driving force behind seeking venture capital was lack of funding for new venture internationalization, but the intrinsic motivations for each INV were
rather different. Internationalization was a primary goal for all of the case companies, and a main reason for raising venture capital. In the case of Chaining, the entrepreneur was first motivated to expand into international markets because of limited domestic sales as well as the ease of applying the products worldwide without many issues or need for technical modifications of products.

Due to the technological nature of the products, worldwide distributor networks have to be built in order to provide installation, maintenance, and after-sales services. High costs are involved in managing such a large distribution network, not to mention the challenge of cultural differences. Placing, Sending, and Basing provide technical solutions that can be easily applied in various foreign markets and do not require any infrastructure. The entrepreneurs from Placing, Sending, and Basing also believed that the Finnish domestic market was not large enough to generate appreciable sales revenue.

Moreover, Sending’s entrepreneur built the company as an international one from the beginning, because he believed no investors would be interested in technology companies that are not prepared for internationalization in this highly globalized world. Basing’s entrepreneur was extremely positive toward new venture internationalization.

Viewing, as a former subcontractor for Nokia, had a clear picture of the subcontractor business in world markets. When Viewing changed direction to focus on the wireless video business, Viewing had already clearly defined the eight largest players in the wireless subcontractor business as the only potential customers in the world market. Viewing had no choice but to follow its customers abroad.

**Case One – Chaining**

Chaining was founded in 2003 and signed its first foreign contracts in 2008. The initial funding was from the entrepreneur, and later on, the entrepreneur invited his former colleagues and friends to invest. The company received seed funding from about ten angel investors plus Finnish government venture capital funding for further development.

Chaining is a special case that failed to raise venture capital as an investment instrument to support the company’s building of an international distribution network. Chaining attempted to negotiate with VC firms, but the needed “relationship chemistry” was lacking, especially for negotiating the terms and conditions in which the venture capitalist would make decisions.
The entrepreneur began to approach VC firms for funding, and the process went smoothly up until the point of negotiation meetings with VC firms. He understood that the early equity investor faces risks and uncertainty about the products, technology, and internationalization, and in response prefers to purchase more shares at a lower price. He was prepared for disagreement regarding valuation of *Chaining* and wanted to negotiate the investment agreement.

However, he was disappointed that all of the VC firms involved in negotiations used a similar investment template developed by the Finnish Venture Capital Association in the early 2010s. He was not able to negotiate freely, due to the strict rules defined by the Finnish Venture Capital Association. He believes that if he had been given the chance to negotiate rather than simply accept the terms and conditions proposed by the VC firms, they might have reached an agreement. He also had concerns about the exit plan and uncertainty about his INV’s future if the milestones set by the VC firms were not reached. He feared that the VC firms would withdraw funding and destroy the future of *Chaining*, similar to a VC-backed story of failure that occurred in his network.

The main reason for not having venture capital in the early stage of the company was an issue of control. The entrepreneur wanted to retain power over the company and guide its direction. He did not want to face a situation in which he was unsure about the company’s future, nor did he want the company to be “exit”, potentially forced out of existence after a merger and acquisition, or to lose control after an IPO.

In general, the entrepreneur behind *Chaining* was not willing to play by the rules of VC firms. He was unwilling to compromise on how to operate the business, how to make decisions on markets to be entered, and what method to use. Being unwilling to cooperate with the VC firms, this entrepreneur ultimately ceased the formation and development of relational capital with VC firms.

**Case Two – Sending**

*Sending* has successfully raised venture capital from a local Finnish VC firm for developing international markets, especially the U.S. market, and the INV is in the process of professionalizing by the VC firm.

*Sending* was interested in both Finnish domestic and foreign VC firms. In *Sending*’s case, as a high-tech startup, it received different kinds of government grants and loans for developing its business in the initial phase. These governmental organizations validated *Sending*’s technology and business strategy in local markets.
and served as a good reference for VC investors. With the governmental funding organizations as references, Sending began networking locally and attracted angel investors in the seed investment phase, then gradually approached both local and foreign VC firms. After participating in different meetings and events and establishing contacts with investors, Sending also undertook the necessary follow-up actions to extend the initial talks with investors. The purpose of all of these activities was to allow the VC firms to get to know Sending better, through both formal presentations and face-to-face communications whenever possible.

When they can be arranged, company visits help make the INV/VC firm relationship closer. Sending’s entrepreneur invited investors for a company visit and listened to their company presentations. Both sides had the opportunity to learn from each other. The entrepreneur will get a bit deeper understanding on VC firm’s daily operation, investment interests, policy and potential capacity for internationalization activities. The VC firm will learn about the company’s products, team and business. The company specific introduction events arranged between Sending and VC firms will create a good feeling between both INV and VC firm, and can be a good start for further discussions and negotiations.

Raising money was not the main purpose of Sending’s quest for venture capital, particularly since the financial position of Sending was quite good at the time of approaching venture capital. The focus was to find the right VC firm that could provide business expertise and scale up the business around the world. Therefore, the choice of VC firm was not limited only to Finland, but also focused on foreign VC firms that were able to increase the valuation of the company. Although Sending attempted to attract international venture capital investment, it has not yet received any.

Sending’s strategy for approaching foreign VC firms was to take part in entrepreneur/investor matchmaking services provided by governmental startup support organizations that existed to compensate for the limited resources and networks of INVs. Sending’s entrepreneur trusted their expertise and the international networks they had built over the years. Because a number of the companies involved in these networking projects offered by public organizations had actually received foreign venture capital, Sending’s entrepreneur was motivated to use the services provided. The government funding also paid for half of the travel expenses and event participation fees. These incentives increased Sending’s willingness to participate in projects, networking, and incubating services provided by third-party organizations. The networking process provided not only the chance
to meet foreign investors, but also increased the company’s presence and credibility in the local business market.

After several rounds of discussion with two VC firms, in 2014 Sending received its first round of investment from a local firm. The entrepreneur had met and connected with multiple VC firms through social networking. He continued to talk only with a small number of VC firms – ones that were interested in Sending and that would bring business competence to his company in the future. He was not interested in investors who only offered money; he expected the VC firms to contribute management know-how to develop international business. The entrepreneur believes that building a relationship with a VC firm goes both ways.

Trust plays an important role in the development of this dyad relationship. The entrepreneur was not willing to reveal his technology know-how to all of the VC firms at the initial phase of discussion. He provided detailed technology information only when the discussions were going well and trust had increased, and after a non-disclosure agreement had been signed. The gradually increased trust transferred part of tacit knowledge of the entrepreneur to VC firms in pre-investment stage.

At the time of interview, Sending had been working with VC firms only for a short period. One of their key value-added services he identified was recruiting a business development manager. Originally, the entrepreneur had wanted to recruit a Chief Financial Officer (CFO), however, the VCs considered a CFO as too high level for developing Sending at the startup stage, not to mention costly for the small company.

Instead, given the job requirements as described by Sending, the VCs suggested employing an internationally experienced business development manager for commercializing and internationalizing the products of Sending. They also proposed a small number of candidates. After internal discussion within Sending’s entrepreneurial team, and based on trust in the VCs, a business development manager was hired. In fact, the entrepreneur was happy with this decision. The disagreement on certain decision had occurred already in an early phase of involvement of VC firm. The solution the entrepreneur believed was to have an open communication and trust on expertise of each other.

Case Three – Placing

Placing was founded in 2012 as a university spin-off. The story of Placing started with the PhD defense of the founder, during which a venture capitalist from an
accelerator joined in. The founder holds a PhD degree and has been a university professor.

The company received venture capital investment in 2014 from an Asian VC firm. Additionally, Placing has received two rounds of seed financing from angel investors in the U.S. and Finland. The entrepreneur believes that relational capital played an important role in obtaining these various financial investments. He actively participated in the Vigo accelerator program, which was supported by Tekes.

Placing was one of the incubating companies of the accelerator Koppicatch. Through Koppicatch, Placing received its first round of seed financing from U.S. angels and Finnish angels. The manager of Koppicatch has close connections with Finnvera, a Finnish government VC firm, with Tekes, and with U.S. angels who have been venture partners of Nokia. These strong connections made it much easier for Placing to raise venture capital for business development. Later on, the entrepreneur raised more venture capital from a Finnish family-owned VC firm after meeting them through a mutual connection. Similarly, Placing’s entrepreneur and team joined Business Oulu’s project to attend a conference in Silicon Valley, where they met an Asian investor.

When connecting to the different investors, Placing’s entrepreneur actively developed relationships with them. He often traveled to the U.S. for face-to-face meetings with VCs, to demonstrate products, and to look for investment opportunities. Once his VC firm A was in place, the entrepreneur felt that this firm increased the credibility of Placing as an investment target and offered a strong signal to angel investors and other VC firms. He was not significantly challenged in terms of scaling up the team or entering foreign markets, having a business model that applies well to all the target countries.

Placing’s entrepreneur put much effort into building and developing the relationship with his Asian investor. He visited the Asian investor’s office more than once to negotiate terms and demonstrate his technology to the investor’s technology team. He invited the investor’s team to visit Placing’s office, have dinner together, and to enjoy small sight-seeing trips around Finland. Because the Asian investor was actively looking for this kind of technology, the deal was actually done within six months of their first meeting.

The entrepreneur believes he was the key person in terms of developing trust between Placing and all of the VC firms. Having a PhD and being a university professor gave him credibility. Further, his personality facilitated open communication along with the ability to gain the needed understanding of Asian
and U.S. culture. Although he felt that the U.S. investors were aggressive, he
remained calm and tactful when responding to their requirements.

One concern of which the entrepreneur was fully cognizant was the potential
to lose control of Placing. He carefully considered this issue before obtaining the
investment. His strategy was to attract as many investors as possible and to give
almost equal shares to every investor, so that no single investor had more power to
make decisions during post-investment activities. He maintained good
relationships with all investors, and if post-investment conflict occurred with an
investor, he would discuss the issue with the others and give the group pressure to
resolve the conflict without harming the relationship.

The entrepreneur acknowledged that the U.S. VCs contributed great effort in
terms of developing the U.S. market and attracting a celebrity from the U.S. to
der endorse Placing – which serves as a good signal and reference for U.S. VCs. In
total, Placing has received four rounds of investment, from seed financing through
startup phase, from various investors. The Asian VC firm is extremely well-known
and powerful in Asia and other countries, e.g., Japan and Korea. With this firm as
a reference, it was easier to conduct international business with other Asian firms.
In Korea, before talking to Placing, the Korean customer had already talked to the
Asian VC firm about the applicability of Placing’s technology and other
information-related issues. Placing’s entrepreneur acknowledged that the Asian
investor had great signaling effects in the Asian market.

Case Four – Viewing

Viewing was able to seize the opportunity that developed the first generation of
wireless video products, and the entrepreneur believes that first-round funding was
easy to get because almost all technology-based companies in the wired or wireless
industries could find the funding required if they had a certain drafted business plan,
regardless of internationalization plans. The entrepreneur believes that the investors
were also opportunistically-minded and eager to be ahead of the curve in new
industries.

In the entrepreneur’s opinion, during the 1990s, venture capital was still a
relatively new concept in the Finnish market, meaning potential investors lacked
investment experience. It was a learning process for VC firms, and they suffered
many losses before professionalizing the industry. Viewing emerged at the time the
Internet industry was booming, positioning it well for gaining first-round funding.
Timing was a key factor influencing relationship formation for Viewing. Besides
the right timing, the entrepreneur’s more than ten years working as a manager of subcontractors for Nokia provided him with many industry connections and inside information regarding the business. The second and especially the third round of funding were difficult to obtain during the downturn of the industry. However, the entrepreneur still managed to obtain the funding from the same investors as in the first round. The entrepreneur emphasized the point that maybe the VCs had already invested so much that they were reluctant to withdraw funding in the middle of the investment process, when the only possible outcome would be loss. The more VCs become embedded in relationship with the INV, the harder it is for them to abandon their funded ventures. Viewing was in this sense lucky, because the VCs still had hope that Viewing could reach exit, albeit with a postponed deadline.

Like the industry, the development of the relationship between Viewing and the VC firm went up and down. Viewing’s entrepreneur appreciated that the VCs were patient during such a difficult time, waited for recovery of the industry, and finally helped Viewing achieve merger with another U.S. company as the exit. The relational capital developed during this time helped Viewing obtain the needed funding and develop the next generation product.

Emotional support from the VCs was also critical for Viewing’s entrepreneur and team, as going through difficulties strengthened the relationship and increased the mutual trust between the two parties. Emotional support and trust might be the most significant contribution from the VC firm in post-investment activities. The entrepreneur did not expect value-added services from the VC firm to contribute to the international business development of Viewing. Thus, the hands-off approach by the VCs and the provision of a sound relationship were sufficient in the case of Viewing.

During the difficult period, Viewing was not able to generate enough revenue to cover all the costs and development of the company. As a result, Viewing lost power in its negotiations with investors. The percentage of shares held by the entrepreneur and key employees dropped to only 14%, which greatly upset the entrepreneur and employees. The third round of funding was the only choice for Viewing to survive, and the entrepreneur had to accept the investment agreement proposed by the VCs. From that point, the entrepreneur perceived that he and the VC firm were no longer in the same boat, but on opposite sides of the negotiation table. Losing control of Viewing changed the entrepreneur’s attitude, motivation, and spirit towards Viewing, and he came to feel that he was just an employee working for the company instead of running his own entrepreneurial company. He stopped caring about the decisions that the board made.
In Viewing’s case, the strong connections with local networks helped Viewing raise venture capital, but only from Finnish investors. Although attempts have been made to approach VC firms in the U.S., due to the distance and lack of presence or a network in the U.S. market, Viewing has failed to raise any U.S. venture capital.

Case Five - Basing

In Basing’s case, they first obtained informal venture capital of 300,000 Euros as seed financing from public support organization Sitra and private angel investors by actively networking in the local market. The entrepreneur said the processes of approaching the angel investors and the VCs were parallel, but separate. Building relational capital was a long process, requiring a great deal of social interaction and networking, such as participating in various events, entrepreneurial training, incubating sessions, and the like.

The entrepreneur believes that timing and personal interactions before the investment decision were the reasons he was successful at raising venture capital. He approached leading VC firms early enough so that they had an opportunity to learn about Basing, the technology, and the entrepreneur. Both the interpersonal and professional traits of the entrepreneur paved the way for the INV to enter the negotiation phase. However, during the negotiation process, the entrepreneur felt that he was pushed into signing the agreement without sufficient time to go through it with the INV’s lawyer. This resulted from either intentionally delayed or accelerated deadlines for negotiations by the VC firm. The entrepreneur realized after term sheet negotiations that all money borrowed would be deducted from the valuation of the company, a factor that greatly surprised and displeased him (interview and secondary data).

In addition to the issue involving the term sheet negotiations, the entrepreneur says that later on, he and the VCs turned out to have different interpretations regarding what had been agreed upon as the company’s base valuation for the second term sheet. Although the entrepreneur tried to set aside any misgivings, he admits that the feeling of unfairness affected the openness of communications and the overall trust relationship. He began to doubt the motives of the VC firm, their abilities, and their willingness to play fair in post-investment activities. As he was an inexperienced young entrepreneur, prone to over-optimism regarding the milestones set by the VC firm and eager to make money, he still decided to sign the investment agreement with the VCs (interview and secondary data).
In post-investment activities, the VCs took a hands-on approach by professionalizing the company and making decisions regarding daily operations. For instance, the VCs were in charge of carrying out and interpreting market analysis and hiring a venture partner for sales in the U.S. Sometimes, the entrepreneur disagreed with decisions made by the VCs, e.g., creating a newer version of the business model and the cost of hiring a new interim CEO, but he felt that he was not able to discuss these issues with them. In the entrepreneur’s opinion, the VCs did not trust his business expertise and considered him only as a technical engineer lacking in international business skills (interview and secondary data).

Since open communication had broken down, the entrepreneur did not learn of situations under discussion or decisions made until the stage of implementation, which effectively denied him the right to influence the decisions made by the VCs. He admits that he might not be as experienced as the VCs at running an international software startup from an international business operational perspective, but he believes he has a superior understanding of customer needs and the future trend of the industry and Internet business.

In most cases, the entrepreneur felt that the timing, location, decisions, or role of the VCs in Basing were not right, based on his tacit understanding of the company’s situation. But due to his limited experience, he did not dare to object or strongly express his opinion. This inexperience and insecurity on the part of entrepreneurs, or their inability to argue with VCs, can prevent optimal cooperation and lead to suboptimal performance between the INV and the VC firm. According to the entrepreneur, it is very important to promote a cooperative atmosphere and constructive discussion, which contributes to developing of trust between the parties (interview and secondary data).

As these kinds of situations occurred during the post-investment stage, the entrepreneur became increasingly dissatisfied with the unevenly distributed fairness, information asymmetry, and lack of trust with the VCs. He lost his motivation to collaborate. As a consequence, the failing relationship between the entrepreneur and the VCs led to the board of directors changing the CEO. The entrepreneur was forced to relinquish ownership of the company. Although he still sat on the board of the company and tried his best to help, the entrepreneur claims that emotionally and mentally, he no longer cared about the company to the point that he began to think of leaving. The change in CEO did not improve the company’s success, and without the involvement of the entrepreneur – with his entrepreneurial spirit, enthusiasm, and tacit knowledge – Basing closed its business with no loss and no gains.
Summary

These case studies exemplify the entrepreneurs’ individual opinions of the relational capital building and utilizing process. The entrepreneurs described the relational capital development experiences with VCs for their own INVs, along with the potential impact of relational capital on their feelings and behavior, as well as on the INV’s future in terms of venture exit. The aim of every entrepreneur was growing their INV in a global context, with or without motivation for internationalization. During this growth process, most of the case companies experienced liabilities of internationalization and needed resources from VC firms. For most of the cases, funding was the most important need motivating the approach to venture capital, with the exception of Sending, which enjoyed a strong financial position. Another main reason the entrepreneurs initiated relationships with VC firms was to obtain value-added services, such as business strategy and internationalization competencies.

The key elements that capture relational capital formation and utilization according to the case stories described by the entrepreneurs are summarized and compared in Table 7. Each individual entrepreneur’s viewpoint on relational capital and its potential impact on the INV’s future in terms of exit are not exactly the same; however, they all felt relational capital played an important role in developing trust with VC firms, that it can improve the likelihood of obtaining venture capital, and that it can contribute to achievement of favorable outcomes.
<table>
<thead>
<tr>
<th>Process</th>
<th>Chaining</th>
<th>Sending</th>
<th>Placing</th>
<th>Viewing</th>
<th>Basing</th>
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<tr>
<td><strong>Internationalization</strong></td>
<td>Market expansion</td>
<td>Technology driven</td>
<td>Technology driven</td>
<td>Customer follower</td>
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<td></td>
<td>Distribution</td>
<td>Limited</td>
<td>Domestic</td>
<td>No other choice</td>
<td>Entrepreneur’s willingness</td>
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<td>market</td>
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<td>Limited</td>
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<tr>
<td></td>
<td>Costs</td>
<td></td>
<td></td>
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<td>domestic</td>
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<td><strong>Motivation for relational capital</strong></td>
<td>Funding</td>
<td>Strategy or value-added services</td>
<td>Funding</td>
<td>Funding</td>
<td>Funding</td>
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<tr>
<td><strong>Starting point of formation of relational capital</strong></td>
<td>Cautious-affected by sad story that happened in Oulu</td>
<td>Match-making events by third party</td>
<td>Events and networking</td>
<td>Venture capital approaching</td>
<td>Telephone approaching to Venture capital</td>
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<td><strong>Factors that affect relational capital</strong></td>
<td>Not able to foresee the future for the INV</td>
<td>Valuation Strategies</td>
<td>Ability to balance R&amp;D and market</td>
<td>Decrease of the shares of key employees</td>
<td>Miss-trust</td>
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<td></td>
<td></td>
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<td>Lay off employees</td>
<td>Non-open communication</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Patient</td>
<td>Conflict on decisions</td>
</tr>
<tr>
<td></td>
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<td></td>
<td></td>
<td>Emotional support</td>
<td>Valuation</td>
</tr>
<tr>
<td><strong>Trend of relational capital when VCs involve(d)</strong></td>
<td>Not Related</td>
<td>So far smoothly</td>
<td>Divided responsibility</td>
<td>Up and down</td>
<td>Decreased</td>
</tr>
<tr>
<td><strong>Exit as performance</strong></td>
<td>Not Related</td>
<td>Not yet Ongoing</td>
<td>Not yet Ongoing</td>
<td>Satisfied, merger and acquisition, it was wise choice</td>
<td>Unsatisfied, due to failure of trust and relationship with VCs</td>
</tr>
<tr>
<td></td>
<td>Managed growth by Revenue-based financing</td>
<td>wait to see</td>
<td>Wait to see</td>
<td>IPO</td>
<td>Business closed. No big loss, no gain</td>
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</table>

Table 7. Individual entrepreneurs’ opinions of relational capital between INV and VC firm during venture capital process
VC firms are clear about the process they use for funding an entrepreneurial company. This subsection describes the efforts and activities that VC firms engage in from approaching INVs until exit, if any, and maps the relational capital accumulated during the venture capital process from the VC firms’ perspective. It also gives insight into their willingness to form relational capital and their expectations of its development, in addition to insight into how VC firms utilize relational capital with portfolio INVs.

As not all VCs from the case companies were accessible, the empirical data from those VCs who did participate is compiled together and presented according to the stage of the venture capital investment process, starting from generating qualified deal flows through exit, if any, instead of being presented on a case-by-case basis. The empirical evidence collected from VC firms offers insight into relational capital in the INV/venture capital context and serves as complementary information to the entrepreneurs’ perspectives.

Because little research has been done on the evaluation of early internationalization of portfolio firms, VCs’ critical thinking about new venture internationalization is based on the empirical data. The major concerns driving the decisions related to new venture internationalization are cost and the abilities of the specific VC firm – that is, whether it is able to offer value-added services and exercise control during the new venture internationalization process after investment. Most of the case INVs approached venture capital early, before their product was ready for launch. VCs’ evaluation of INV applications was therefore based on the question “who will buy the products” (according to a venture capitalist for Placing), which led to the VC firms putting more effort into evaluating the salesperson or sales team that would be responsible for developing international markets. If the salesperson or team were not available, the VCs’ next approach would be to evaluate their own operations in terms of whether they had an appropriate candidate in their network, in the relevant industry, who could later be hired by the INV to guide internationalization after investment. This option requires the cooperative understanding of the entrepreneur. In fact, this scenario actually occurred in the internationalization process of Placing.

In the case of Placing, the entrepreneur and the Oulu-based team were only responsible for R&D. The investors had shaped almost all of the strategies with regard to business operation and early internationalization. The U.S. VCs were the driving force behind the internationalization process of Placing, and, because they
had the business expertise and close connections in the U.S. market, they helped Placing secure the first contracts with airports and supermarkets in the U.S.

The next direction was for Placing to enter the Korean market. The Placing’s advisor believes that the Asian corporate venture capital investor, was the catalyst for this entry decision. Although business expertise was lacking in Placing in the beginning, before investment, Placing appeared so promising that the VC firm felt it was worth the associated risks. After all, the primary motivation behind VC firms’ funding decisions is “return on investment.”

The VC firms participate in various events and activities to generate highly qualified deal flow. They also actively cooperate with each other and with third parties such as incubators, business support organizations, and universities. The formation of Placing was steered by a venture capitalist who listened to the doctoral defense of the entrepreneur. The venture capitalist was interested in new technology developed from the research project and talked to the doctoral candidate about the potential of applying the technology to a real business. With discussion and the help of the venture capitalist, the doctoral candidate became an entrepreneur and established Placing. This was the starting point of the emerging relationship between the INV and the VC firm. Placing has received three rounds of investment thus far, and for the second and third rounds, another U.S. VC firm joined in, one that actually became involved through the network of investors from the first round.

The VCs claimed that angel investors played an important role in professionalizing Sending’s business strategies and commercializing their products, both of which helped Sending become investment-ready for VCs. Sending has already signed the first contract with a Swedish maritime company, which shows the clear potential for international markets. The VCs believe that Sending’s early internationalization is not especially risky, because the team is composed of professional, smart young adults who can quickly react to change and learn fast. Moreover, the contract with the Swedish customer serves as a positive signal for new venture internationalization in terms of future venture capital decisions.

According to the VCs, the angel investors also participated in negotiation meetings with the entrepreneur and VC firms to discuss the business model, international business plan, and investment agreement. The angel investors have not yet exited from Sending; instead, they became the syndication partner of the VC firm. The continuous investment by angel investors demonstrates the smoothness of the relationship between the entrepreneurial team and the angel investors and indicates the willingness and ability of the entrepreneur to deal with external equity partners.
From the investors’ point of view, the relationship with Placing’s entrepreneurial team sometimes does not work so well, as the entrepreneur’s team members are purely technology-focused and hold master’s and doctorate-level degrees in their field. They are not particularly suited to international market exploration and business development. The investors therefore have to drive that effort and take the main responsibility for developing new markets and securing contracts with customers.

Cultural differences also are encountered by the Finnish entrepreneur and the U.S. investors of Placing. Fortunately, since the U.S. investors were ex-Nokia general partners, they have worked with Finns and understand their way of doing business and developing startups. This background of the U.S. investors is quite possibly the reason behind the successful raising of venture capital from U.S. VCs. In addition, the U.S. investors already were prepared before making their investment decision to be in charge of business development for Placing, resulting in no surprises related to Finnish business culture and communication with Finns. In this way, the investors’ experience in Finland helps to solve problems, handle conflicts, and avoid misunderstanding in post-investment activities. It also demonstrates how important it is to approach the right VCs in the pre-investment stage.

As Placing’s advisor said, without the help of the U.S. investors, Placing would have built up the business as do other Finnish startups, following the slow and ordinary steps that heavily focus on R&D. She further elaborated that the focal point for U.S. investors is the market and trying to build Placing as big as possible for an IPO.

The Finnish approach and the U.S. approach are rather different. Some conflicts and cultural differences inevitably occur during the investment process. However, due to mutual understanding and sustainably developed relational capital, entrepreneur and VCs have agreed on the division of tasks. The quality of the relationship increases trust in each other’s strengths so that compromises can be reached.

The U.S. investors trust the Finnish team’s R&D capabilities. On the other hand, the Finns trust the business expertise of the U.S. investors. The Finnish team, led by the entrepreneur, conducts research and improves the products available for the markets. The U.S. team, a group of VCs and angel investors, pursue market development and search for the next round of financing. In fact, the U.S. investors successfully made the investment deal with Asian investor in Asia through their network connections.
Overall, development of Placing is proceeding well, resulting in various kinds of rewards and achievements in the post-investment process. The U.S. investors claim that they have contributed great effort to increasing the valuation of Placing through their hands-on approach and involvement in daily operations.

Summary

As not all the case INVs’ VCs were accessible – whether due to the age of the venture, the departure of the key person from the VC firm, or unwillingness to participate in the research – the VCs’ perceptions of the role relational capital plays in working with INVs is illustrated collectively in Table 8.

Table 8. VCs’ collective understanding of relational capital with INVs

<table>
<thead>
<tr>
<th>Process</th>
<th>VCs’ perspective</th>
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<tbody>
<tr>
<td>Internationalization</td>
<td>Cost, risks, International market potential</td>
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<tr>
<td></td>
<td>Business competence for delivery in foreign markets, by the INV</td>
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<td></td>
<td>or help of Venture capital (signaling effects)</td>
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<td></td>
<td>Return on investment, US process for building as “big” as possible</td>
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<tr>
<td>Motivation for formation of relational capital</td>
<td>Highly qualified deal flows</td>
</tr>
<tr>
<td>Formation of relational capital</td>
<td>Networking in events and activities</td>
</tr>
<tr>
<td></td>
<td>Introduced by other Venture capital general partners</td>
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<td></td>
<td>Negotiation meetings</td>
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<tr>
<td>The role of relational capital before Venture capital decision</td>
<td>Obtaining information withheld by entrepreneur</td>
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<tr>
<td></td>
<td>Understanding of team in detail</td>
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<td></td>
<td>Cooperative willingness under control</td>
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<tr>
<td>The role of relational capital after Venture capital decision</td>
<td>Accelerated learning process</td>
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<tr>
<td></td>
<td>Goal incongruence</td>
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<td></td>
<td>Conflict resolution</td>
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<tr>
<td>Factors that affect relational capital</td>
<td>Control</td>
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<td></td>
<td>Cooperative manner in conflicts</td>
</tr>
<tr>
<td>Exit as performance</td>
<td>Failure by closure – in Basing</td>
</tr>
<tr>
<td></td>
<td>Success by merger and acquisition – in Viewing for good ROI</td>
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<tr>
<td></td>
<td>Expected exit – US process for building it as big as possible - IPO</td>
</tr>
</tbody>
</table>

Table 8 illustrates that the attitude toward new venture internationalization is conservative in nature, given the consideration of the costs and risks associated with internationalization. VC firms can also be very aggressive and opportunity-driven if they are skilled at helping INVs develop international markets. The key
purpose of forming a relationship, from the venture capitalist’s perspective, is to acquire information from the entrepreneurs as well as keep them motivated to offer sweat equity during post-investment activities. The VCs understand the importance of building and utilizing relational capital for aligning goals and achieving better performance results and ROI.

5.2.3 Comparisons between the two groups

Table 9 concludes the description of the individual stories of the entrepreneurs and the collective viewpoints of VCs by identifying the similarities and differences of motivation and the expected outcomes of relational capital. The starting point was new venture internationalization.

The common thread of thought between the two groups was the limited size of the domestic market and the features of the products that made internationalization possible. However, while the entrepreneur considers new venture internationalization an opportunity, the VCs see internationalization as associated with many risks and costs. From the entrepreneurs’ perspective, they need capital for international expansion and added capabilities to execute international business operations. From these two standpoints spring the motivation for forming relational capital: to increase mutual understanding and reliance on each other’s competence.

For both groups, the way to build relational capital begins with active networking and recommendations from referrals. The key factors that affect relational capital building process are the valuation of the INVs, as the entrepreneurs and VCs hold different perceptions on internationalization and recognition of their ability in doing so. Once the investment agreement has been signed, the purpose of utilizing relational capital is to achieve better internationalization performance results and to achieve the alignment that serves the best interests of both parties. Entrepreneurs expect valuable references and network resources from VCs, and for their part, VCs demand more information from INVs and push to exit for their ROI.
Table 9. Comparisons between entrepreneurs and VCs’ perspectives

<table>
<thead>
<tr>
<th>Process</th>
<th>Similarities</th>
<th>Differences</th>
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</thead>
<tbody>
<tr>
<td></td>
<td>Entrepreneurs’ perspective</td>
<td>VCs’ perspective</td>
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<tr>
<td></td>
<td>Cost and risks</td>
<td>International market potential</td>
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<td></td>
<td>International market potential</td>
<td>Business competence for</td>
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<tr>
<td></td>
<td>Lack of funding</td>
<td>delivery in foreign markets, by</td>
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<td></td>
<td>Lack of network in international market</td>
<td>the INV or help of Venture</td>
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<tr>
<td></td>
<td>Cost and risks</td>
<td>Return on investment</td>
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<td></td>
<td>U.S. process for building as “big” as possible</td>
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<tr>
<td></td>
<td>Motivation for formation of relational capital</td>
<td>Highly qualified deal flows</td>
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<td></td>
<td>Starting cooperation</td>
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<td></td>
<td>Getting connected</td>
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<td></td>
<td>Passing evaluation</td>
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<td></td>
<td>Getting funding for INVs</td>
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<td></td>
<td>Formation of relational capital</td>
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<td></td>
<td>Active networking</td>
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<td></td>
<td>Company presentations</td>
<td>Introduced by other Venture</td>
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<td></td>
<td>Third party involvement</td>
<td>Capital general partners</td>
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<td></td>
<td>“signal” from Angels</td>
<td>Negotiation meetings</td>
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<td></td>
<td>Power in negotiations</td>
<td>Obtaining information withheld</td>
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<td></td>
<td>Quick decisions</td>
<td>由 entrepreneur</td>
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<td></td>
<td>The role of relational capital before venture capital decision</td>
<td>Understanding of team in detail</td>
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<td></td>
<td>Information exchange</td>
<td>Cooperative willingness under control</td>
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<tr>
<td></td>
<td>Shares hold by entrepreneurs</td>
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<td></td>
<td>Controlling liabilities and cost</td>
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<td></td>
<td>True value-added services</td>
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<td></td>
<td>Valuation</td>
<td>Able to monitoring</td>
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<tr>
<td></td>
<td>The role of relational capital after venture capital decision</td>
<td>Controlling liabilities and cost</td>
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<td></td>
<td>Better performance</td>
<td>Culture background</td>
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<td></td>
<td>Next round funding</td>
<td>Accelerated learning process</td>
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<td>Compromises</td>
<td>Goal incongruence</td>
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<td>Power</td>
<td>Conflict resolution</td>
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<td>Emotional support</td>
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<td></td>
<td>The role of relational capital after venture capital decision</td>
<td>Failure by closure – in Basing</td>
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<td></td>
<td>Exit as performance</td>
<td>Success by M&amp;A – in Viewing for good ROI</td>
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<tr>
<td></td>
<td>Success</td>
<td>Expected exit – IPO Placing, wait to see for Sending</td>
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<tr>
<td></td>
<td>INV is still under entrepreneur’s control</td>
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</tbody>
</table>
As a general conclusion, while both entrepreneurs and VCs see the importance of relational capital to achieve better internationalization performance results, the motivation behind building and utilizing relational capital may be very different.

5.3 Capturing the formation of relational capital

The prior subchapter presented and summarized individual entrepreneur and venture capitalist viewpoints on relational capital in each case company, and made clear the motivation, importance, influence factors and consequences of the emergence and development of relational capital between the INVs and VC firms. This subchapter discusses the important factors that affect the formation and utilization of relational capital in the venture capital investment process, as well as the meaning of relational capital for entrepreneurial INVs and VC firms. The potential links between each factor and impact on the venture capital process are further explored from empirical data. Finally, the factors discovered in the data that might influence the emergence, development, or even clash of relational capital between INVs and VC firms in new venture internationalization are presented.

The purpose of data analysis is to understand the real situation of relational capital in practice from both entrepreneurs’ and VCs’ viewpoints, then to generate an overall understanding of relational capital in the venture capital investment process for achieving the goal of new venture internationalization. For the analysis, the five cases serve as a background. The analysis does not directly compare entrepreneurs’ and VCs’ perceptions within each case. Instead, the comparison is contemplated through identifying similar and different understandings of relational capital for INVs between entrepreneurs as one group and VCs as another.

5.3.1 New venture internationalization

All of the case companies internationalized very shortly after inception, within six years of establishment, and demanded funding and resources at the initial phase of early internationalization. However, the driving forces and motivations for internationalization of each case company were not the same. VCs may assess new venture internationalization with their own views and criteria. This subsection empirically shows the perceptions of new venture internationalization from entrepreneurs’ and VCs’ viewpoints.
Entrepreneurs’ perspective

As VC firms tend to be more interested in high-tech sectors, all of the case companies were or are currently operating in high-technology industries. All of the entrepreneurs interviewed hold at least a master’s degree in technology. None had any business education at the point of venture establishment. Their motivations and driving forces for internationalization were not all the same. The following statements illustrate the reasons for early internationalization as well as the risks and challenges that the entrepreneurs foresaw before making early internationalization decisions.

“Internationalization is based for making papers and giving training, and doing cooperation in more market and sales, and I do not see so big risk if we choose wrong distributor, because they do not own the exclusive right for the first time. We have 150 partners and they have 250 locations. There are more than 20 partners selling our products. We are not giving exclusive for them.” (Entrepreneur – Chaining)

“Internationalization is always risky, and operation goes hand-by-hand, side-by-side . . . Everybody knows that in Finland, the market is very limited, so having a company operating in Finland and having remarkable revenue is really hard, and so therefore going international is the only way to grow the company large enough to become the interesting investment target.” (Entrepreneur – Sending)

Sending’s entrepreneur delivers the message that the Finnish market is not large enough for developing the company, which forces Sending to internationalize early. On the other hand, internationalization provides opportunity for new ventures to grow big enough to attract venture capital investment.

“I see internationalization as an opportunity, not necessarily the risks associated with higher costs. I don’t personally agree with the differences between international or non-international firms. There is also my background as an Internet entrepreneur; none of the ideas we looked for financing for we thought as domestic, each and every single one of them were ‘born global.’ The only way to achieve growth for the new venture is to internationalize, and some business, especially in high-tech, depends on business models which cannot
‘live’ without internationalization, and, depending on the markets, whether to do it globally or not at all. In this respect, the aspiration for global markets, especially in Finland, is the key trigger, whether there is a venture capital case or not.” (Entrepreneur – Basing)

This comment from Basing’s entrepreneur shows that the entrepreneur’s global mindset and his confidence in the technology enabled the new venture to achieve first-mover advantage in the Finnish domestic and U.S. markets, and to gain business expertise regarding how to operationalize internationalization. Besides the limited domestic market and features of the Internet industry, the global mindset makes the entrepreneur believe that the only possible way for venture growth is to actively operate in international markets.

“The whole semiconductor industry is quite precise, and there was not a huge amount of players, because huge amount of investment was needed in this industry. If I remembered (correctly), during 2002–2008, eight players around the world conquered 86% market shares of manufactures. Our products were very specific in the way that only fitted to these eight players. We only needed to build bridges between Viewing with those players.” (Entrepreneur – Viewing)

The comment from Viewing’s entrepreneur demonstrates that Viewing became involved in foreign markets as a customer-follower. In fact, for Viewing, there was no other choice but to internationalize early to provide services and solutions for foreign customers.

Based on analysis of the above-mentioned comments, the most-cited reasons for choosing early internationalization are technology, nature of the product and limited domestic markets. The choice of new venture internationalization also should be recognized as one driven by the passion and enthusiasm of the entrepreneurs for developing the business. The entrepreneurs’ attitudes toward internationalization are positive; each considers new venture internationalization as an opportunity rather than being overly concerned about the risks. The reasons for their lack of awareness of the liabilities of early internationalization might be lack of international business experience, lack of expertise in the initial phase of the new venture, and overconfidence in technology and products. The process of new venture internationalization for technology entrepreneurs is very much “learning by doing.”
Sending’s entrepreneur intentionally structured the company from the very initial phase to be a global one. He explains that early internationalization might increase the potential of obtaining venture capital, because internationalization is one way to position a new venture as an interesting investment target, according to the conversations he has had with various investors. He elaborates further:

“Everything we have been doing is for global market. It is basic assumption that investors expect us to go abroad . . . Based on conversation we had (with VCs), I have a feeling that almost all the investors in Finland looking for the companies go international . . . VC firms know it is a big risk that takes a lot of work, but the other side, return, is very high, and they are willing to take this risk . . . For funding up and scale the business only for Finnish market is impossible.” (Entrepreneur – Sending)

Each case company chose different operational models for internationalization and drafted a detailed plan for the company. This is a good starting point for attracting VC firms. No matter what drove case companies’ internationalization, they were well prepared for early internationalization based on their own experience and understanding of what markets to enter:

“We must use foreign distributors for installations and maintenances. It is impossible to use our own staff to do these activities worldwide . . . The focal market is Europe, but we plan to expand the activities in Asia and North America in the near future.” (Entrepreneur – Chaining)

“Because from early stage of the company we have clear plan to going international, it is not like we are lack of plan, and going here and there . . . We start from nearby country, Sweden.” (Entrepreneur – Sending)

“We should have the focal market, and we believe Silicon Valley, USA, is one of the Internet-based technology districts that allow us to develop the technologies and find enough promising customers.” (Entrepreneur – Basing)

“The first foreign office we built was in Japan because of the signed deal with that Japanese company. In order to better serve the customer, we decided to build Japanese office. The office in Silicon Valley, U.S., was also established, because we wanted to approach U.S. VCs during the Internet bubble in 1990s.
Without presence in U.S. market, it was difficult to get customers and funding.” (Entrepreneur – Viewing)

The preceding quotations demonstrate the entrepreneurs’ vision regarding the choice of markets and strategy in relation to new venture internationalization, based on the entrepreneurs’ understanding of the situations of selected case INVs. A clear internationalization plan serves as a starting point for knocking on the doors of VC firms.

VCs’ perspective

The motivations behind and decisions made by entrepreneurs regarding new venture internationalization are mainly from the perspective of technology, or R&D, instead of financial and market considerations. Instead, the VCs emphasize the risks and challenges that accompany the internationalization process.

“Investing in a project that involves early internationalization increases a lot the risks, both operational and financial, because a small team might not afford the complexity of management of such a process, as well as the big costs you have for the internationalization process.” (Venture capitalist – Italy)

“VCs may have a different mindset regarding internationalization. I mean, we are willing to invest in industries and companies we are more familiar with and in which we can add more value in terms of our personal network of contacts that can easily open new markets. We think that timing, risks, and the financial resources involved, and the typology of strategy related to internationalization is important. We should learn more about new venture teams and their capabilities for internationalization, and whether we are able to exercise control after investment.” (Venture capitalist – Italy)

“We see that internationalization as a strategy for venture growth may be more important when it comes to startup and growth venture deals. As far as seed projects are involved, what is more important is the scalability of the project, namely, the easiness to copy/paste the business into other countries without replicating all the costs.” (Venture capitalist – Placing)
These remarks highlight a common understanding shared by most VC firms: new venture internationalization not only creates operational risk, but also brings financial costs from the resource-based viewpoint.

VCs may also consider internationalization as an opportunity when internationalization is the only way to achieve growth of the company, and when the technology allows the company to enter foreign markets, especially in Finland, as was the case in Sending:

“It is naturally internationalization product, (which) is not needed in Finland. At least it is in the Finnish soil, and international market, not much choice. Industry for sure was the primary consideration for selling abroad. Obviously, we started from nearby countries, companies that operate in long distinct vessels.” (Venture capitalist – Sending)

Summary

To sum up, the opinions of whether a new venture should internationalize right after inception were different from the entrepreneurs’ and VCs’ perspectives. Entrepreneurs are concerned with internationalization as a strategy mainly because of the nature of products driven by technology. They are confident about their technology, sometimes over-confident, and may neglect to consider resource deficiency and other market risks associated with internationalization. None of the entrepreneurs mentioned risks. For the risk- and challenge-related question asked during interviews, most entrepreneurs believe that the challenge of early internationalization is related to technology of the company. Only one entrepreneur from a case company has seen how internationalization can lead to high cost, due to the need to establish large distribution networks worldwide:

“It’s quite expensive to build up the brand of our own in new countries and to let people know your company and trust your brand. It is quite expensive task to managing a large of distributors’ networks.” (Entrepreneur – Chaining)

Most of them feel the only way to survive and succeed is to internationalize, due to the nature of their products and the limited domestic market. Overall, most of the entrepreneurs are rather positive toward internationalization and expect high growth in international markets for their business. Some are succeeding and some are not, with and without venture capital investment.
On the other hand, the VCs’ primary considerations are the scalability of the business, markets, and potential financial resources needed for internationalization, and the risks associated. They are willing to invest in international new ventures only when the business is controllable, such as with an internationally experienced team. Desire for good return on investment is among the most important reasons for funding an INV. As the consequences, the abilities of entrepreneur in execution of internationalization process play an important role in assessment in deal evaluation process.

The different perceptions between entrepreneur and VCs toward new venture internationalization might result in conflicts of interest between the two parties, and might affect the formation and development of relational capital in the later phase of the venture capital investment process.

5.3.2 Appropriate referral

Referral plays an important role in bridging entrepreneurial INVs with VC firms, especially at the deal origination stage. Deal origination is a two-way process that connects entrepreneurial startups with VC firms. Receiving a referral can be achieved through having a good record of working with publicly funded, governmental organizations or through attending various events and activities.

Entrepreneurs’ perspective

Most of the entrepreneurs in Finland feel challenged to obtain investment from VC firms due to the limited amount of venture capital available and strong competition among technology startups in Finland. With this kind of situation, entrepreneurs are highly motivated to attend different events, extend existing networks, and build new ones to gain referral to a list of potential VC firms:

“It was very easy to obtain the governmental funding, and we were part of Vigo program of Tekes, and incubated by the accelerator that had close connections with Finnvera and Tekes and angels from Finland and U.S. Of course, we also had a great story to sell.” (Entrepreneur – Placing)

“In those events (Money talks, pitching, business conferences), we have been met some people. They have introduced us to some others, and we started networking.” (Entrepreneur – Sending)
“Knowing people is important for business. By networking, like in seminar, entrepreneurship events, I get to know Sitra people, and they get to know our business, so Sitra as one of the key investors helped me to connect with other angel investors.” (Entrepreneur – Basing)

The comments from entrepreneurs represent the importance of knowing people through actively networking prior to approaching VC firms. Networking activities make it possible for the entrepreneur to directly connect with and develop relationships with different kinds of investors, including public investors, angels, and VC firms.

As a subcontractor for Nokia, Viewing had been deeply involved in the network of the wired and wireless industries, which provided opportunities for the entrepreneurs to gain extensive experience. The process of pursuing venture capital started with identifying potential VC firms among the industry networks of Viewing:

“The [entrepreneur A] knew the existing networks, and within these industrial networks there were a lot of players that have already invested by VC firms. He knew the VCs not very well, but by names. He knew what are the funds and funding activities, and it is very easy to get [VC firm A] as a partner. [VC firm B] was another old Finnish family-based business fund. Few others more funds, or private investors were also accessible.” (Entrepreneur – Viewing)

The entrepreneur’s industry network became the information channel through which he found the benchmarking models for Viewing. Those benchmarking models provided the guidance for the entrepreneur to approach the right VC firms.

Both Sending and Placing participated in projects and training programs organized by public support organizations. One particular project was designed to support new venture internationalization and match the selected ventures with investors through their networks. Obtaining venture capital domestically and abroad was also part of the project:

“. . . but some like Finpro and public supportive organization and that kind of institutes working for the companies, so basically that kind of institution doing the basic work finding the candidates and meeting, and match investors . . . they have better networks than we have. Because we are just startup as a new small company, finding investors is already quite big work, if there is someone
know the industry and network and just introduce the company to investor, and that phase we are very pleased to use that services.” (Entrepreneur – Sending)

“Public supportive organization has selected Placing into the project related to pitching in U.S., and public supportive organization paid half of the travel costs and all conference participation fees. In the pitching event or conferences, Placing met the initial U.S. venture capital investor.” (Advisor – Placing)

Sending’s entrepreneur trusted and relied on their network to find potential investors. Participation in projects organized by third-party organizations also saved costs related to searching for investors and potentially increased the number of matches between INVs and VC firms. As the advisor described, Placing joined this project and was fortunate enough to gain investment from the U.S. VC firm. Being referred by a third party, especially from a public support organization or angel investor, was the best way to increase the credibility of the INVs:

“Start up aid and loans from keksintösäätiö and Tekes prove the working of the technology and ability of the entrepreneur to exercise on the drafted business plan. It gives the positive signals to the venture capital investor.” (Entrepreneur – Sending)

“Public supportive organization helped Placing to shape their internationalization strategy, and increases the visibility of Placing in the market.” (Advisor – Placing)

“Angel investors and VC investors mutually . . . attract the second and the third VC firm for the next round financing.” (Advisor – Placing)

The comments above indicate that other outcomes related to referrals were to shape business strategy and professionalize the INVs. Interestingly, only Basing’s entrepreneur did not agree that angel investment had affected the likelihood of being invested by the VC firm. He thought it was a parallel process in approaching these two early-stage equity investors:

“Contacting and discussing with VC firm [which became the lead investor for Basing] started all before obtaining the seed financing from angel investors.” (Entrepreneur – Basing)
Although initial contact with VC firms was made before receiving funding from the angel investors, according to the timeline of receiving different kinds of investment described by the entrepreneur, the seed investment allocated from angel investors occurred before the venture capital decision. The entrepreneur elaborated:

“To a certain extent, angels helped Basing to negotiate with VC firms as well as doing a follow-on investment at the same time with VC firm.” (Entrepreneur – Basing)

His comments indicate that angel investors did not connect Basing to the VC firm at the initial phase of approaching venture capital, but as he realized, the angels did have a positive signaling effect on the later phase of the venture capital process. At the very least, the round of angel financing definitely improved Basing’s credibility and, as an aspect of relational capital, Basing was able to demonstrate their potential to VCs. Basing’s entrepreneur believes that referral might or might not play a role in the deal origination phase, but involvement of angel investors can have signaling effects on later negotiations and the deal structuring phase. His thinking is consistent with that of the VCs and advisors:

“The angels have professionalized Sending and increased the valuation of the company very much before venture capital investment. The angels also participated in part of negotiation meetings on behalf of Sending.” (Venture capitalist – Sending)

“Angels have helped us in finding a famous person from U.S. When he joined the company, it increases credibility of Placing to VC firm in U.S.” (Entrepreneur – Placing)

“He works for Placing until now as a COO. He was a great angel for Placing who not only put his own money for his own salaries, but also explore the market opportunities and pull another investors into Placing. (For example) He was the person behind the massive media presence of the firm, which increases the image and visibility of Placing in the markets.” (Advisor – Placing)
The referrals, especially the angel investors who professionalized the company, contributed to increasing the valuation of the firm, which led to the INV’s having more power in negotiation with VC firms. Moreover, angel investment in the case companies provided VCs with a positive reference indicating willingness on the part of the entrepreneur to collaborate and share control of the funded venture. It also demonstrated the abilities of the case entrepreneurs to work with external investors.

**VCs’ perspective**

A quote from the venture capitalist interviewed in Italy properly introduces the motivation for formation of a relationship early on with startups:

“VC firms are also competing with good investment companies, and it goes both ways, and not just startups apply.” (Venture capitalist – Italy)

This comment reflects how important prospective investment proposals are to VC firms. The formation of relationships with startups occurs on various occasions. Like entrepreneurs, VC firms also actively participate in events and activities organized in the local community and extend their networks to discover qualified investment proposals. Participation in an event organized in the U.S. made it possible for the U.S. venture capitalist to meet the entrepreneur of Placing and begin a business relationship.

“One of the U.S. investors knew Placing through company’s presentation in the business conference held in New York City, U.S. He got immediately interested in the product prototype . . . Another reason for commencing the talk between the entrepreneur and the venture capitalist was also the work experience that the venture capitalist had in Nokia for the past ten years.” (Advisor – Placing)

Through active networking, VC firms are able to find highly qualified deal flow and build relationships with prospective startups. Relationship formation occurs not only during formal business events and activities, but also through daily activities, such as common leisure time hobbies as described by Sending’s venture capitalist:
“I think I met the guys before I knew what they were doing. During a sort of the first initial round of discussions, I obviously had a chance to get to know them better, and since then, we all knew and realized we were skiers and climbers and we all sort of saw each around on both of types of occasions (leisure activities). This was a sort of informal part that established a good feeling towards the personal level of trust.” (Venture capitalist – Sending)

The leisure activity provided the chance for the venture capitalist to understand the entrepreneur as a person: his personality, ambitions, and attitude toward life. This opportunity to develop a deeper relationship gave both parties the ability to test early on whether they could work well together, in addition to fostering good feelings for future investment cooperation. These activities also are the beginning of building relational capital, which again does not only start in formal business occasions. As the venture capitalist from Sending mentioned, social activities also increase the personal level of trust.

The most trusted way of finding investment proposals is through recommendations by partners within the VC firm’s network. Placing received a total of three rounds of investment from multiple VC firms including Finnish, U.S., and Asian firms.

“It is all about your network. I was introduced to the company by a venture capitalist by VC firm A. He found a company and he was listening to the presentation in the PhD defense, that’s how he come across the company. He said, you know, we can found a company around your research work. VC A from VC firm A is an investment firm already in Helsinki and helped launch and start Placing. The VC A was a colleague at Nokia Ventures, years ago in 90s, made introduction to me.” (Venture capitalist – Placing)

Connections from both personal and business lives help create a level of trust between startups and VC firms, leading to formation of relationships if the interest continues between the two parties. The VC firm can also find prospective investments through other trusted VC firms or third-party organizations, which is the most reliable and least expensive way.

Similarly, referrals not only introduce potential deal flows to VC firms, but also can speed up the process of evaluation. Sometimes, VC firms rely on other VC firms’ expertise to make fast investment decisions:
“I should tell you this; we have a trusted partner with us that is a VC firm A of Helsinki. I work with the venture partner, and I know that venture partner for close to 20 years. So there is a trust, and then that makes it happen a lot of easier. But we still need to go through around our process. We have a partnership and we have an investment committee, so we still need to do the intelligence, but it still made it a lot of easier.” (Venture capitalist – Placing)

With regards to time frame after Placing was introduced until investment decision made, it lasted only less than half a year from June to October 2012 by that U.S. VC firm. This contrasts with Basing, in which the same investment decision-making process required more than two years. This seems to indicate that establishing a quality relationship with a new venture takes much more time than being introduced by a trusted partner. In the former case, much time is spent on getting to know the INV, validating technology and the market, as well as getting to know the entrepreneurial team. Overall, referrals by trusted partners can speed up the venture capital decision-making process.

Summary

To conclude, the empirical data indicates that from the entrepreneurs’ perspective, referral plays an important role throughout the venture capital process in forming relational capital with VC firms. First, referrals introduce INVs to potential VC firms. This is achieved through actively networking within an industry. Relational capital helps the entrepreneur to initiate discussions with VC firms. Second, referrals have a signaling effect on initiation of relational capital with VC firms. The signaling effects in data refer to an acknowledgment of technological know-how, the entrepreneur’s ability to execution of business plan, and the ability of the entrepreneur to work with external investors. These effects may help the INV pass the deal evaluation phase of venture capital investment. Third, the referral, especially angel investors, may become involved in negotiating with the VC firm on behalf of the INV. Moreover, nurturing by angels may also increase the valuation of the INV, leading to greater negotiation power and the potential for the INV to receive venture capital in the deal-structuring phase.

In the opinion of VCs, the emergence of relational capital with new ventures in the deal origination phase starts with actively networking, much the same way that entrepreneurs operate. Networking activities are not limited to formal business meetings. As with one of the case companies, even participation in a doctoral
defense can reveal business ideas and give rise to an INV that could become an interesting investment target. The most reliable way to form a relationship with the prospective investment is through referral, especially from investment partners. Deals recommended by trusted sources reduce the cost of information, including searching for investments and building and developing costs. Information on the recommended deal is easily available through trusted venture partners, which accelerates the process of deal evaluation.

In conclusion, the more mutual connections INVs and VCs have, the more likely it is that they will be introduced to each other. Relational capital is formed purposefully between INVs and VC firms, either for attracting interest to an investment proposal or for generating certified deal flows.

### 5.3.3 Interaction between INV and VC firm

In this study, interaction is defined as “mutual or reciprocal action where two or more parties have an effect upon one another.” For the case companies, connectivity – an inherent aspect of interaction – has already been established, either through actively networking or through referrals. The purpose of interaction between INVs and VC firms is to achieve an investment agreement and value creation.

**Entrepreneurs’ perspective**

The connection with a VC firm is just the beginning of a relationship. Follow-up interactions start the formation of relational capital. *Placing* had connected with VC firms from Finland, the U.S., and Asia before actual interaction started through referrals. The entrepreneur was extremely active and kept cultural issues in mind.

“At personal level, I invited them to our office and had dinner in Oulu and arranged small trips around Finland. I always feel personal relationship is important for doing business. At company level, I tried to meet investors as often as possible, made travels to U.S. and Asia to start deep dialogs with VCs about technology and scalability of Placing.” (Entrepreneur – Placing)

After *Sending’s* entrepreneur met the VCs, he started to interact with them by emailing, and invited them to visit the company:
“Later on, when the timing was right, I just directly sent emails to them (VCs) and say could you talk it to me? . . . The frequency of interactions depends . . . Maybe once in a month, of course, if there are some negotiations ongoing, we meet even once a week.” (Entrepreneur – Sending)

“Inventing VCs to visit company helps to increase understandings on what we are doing.” (Entrepreneur – Sending)

Sending’s entrepreneur initiated the relationship with VC firms. Of course, not all of his emails received a reply. However, when he did receive a positive reply, it offered an opportunity to arrange presentation and negotiation meetings. The process of developing a relationship with the VC firm might take a long time – including formal presentations and company visits – in the absence of references. Basing went through almost the same process as Sending. It took about two years before the investment decision was made, as Basing’s entrepreneur explains below.

“At the same time, we started to approach VC firm A in 2004 by telephone to show our willingness to obtain venture capital and followed this by a business plan presentation and negotiations. I established a long-term relationship with VC firm A until the first-round investment was allocated in 2006. Within these two years, we often talked about businesses and the performance of the venture in formal meetings and also at social occasions that help to develop trust. After two years of interaction, I believe, VCs knew us pretty well before the first-round investment decision was made in 2006.” (Entrepreneur – Basing)

According to Sending’s and Basing’s entrepreneurs’ experiences, the frequent formal and social interactions strengthened the relationships between entrepreneurs and VCs. During interaction, a key aspect of relational capital – trust – was created, as Sending’s entrepreneur describes below.

“At the very first meeting, we just need to approve that the technology is working, and we don’t need to talk technology in details, about business plan. We can keep it on the high level. Then, if the negotiations keep on going, we will sign the non-disclosure agreement with investors, and goes on details.” (Entrepreneur – Sending)
Interaction between INVs and VC firms is an information exchange process, through which both parties learn to each other and develop trust. Sending’s entrepreneur explained “interaction” as a time-consuming but essential process of information exchange:

“The first meeting is just very normal to change the idea at an abstract level. And if the investors interested, more and more negotiations are ongoing in details and such. Those negotiations take quite a lot of time to get someone understand the business and [be able to] change the idea, to make the assumption on the valuation and investment, and to see whether anything to offer, [including] not only capital investments, but also potential competences to us.” (Entrepreneur – Sending)

Sending’s entrepreneur explained that interaction allowed both parties to exchange information and transfer knowledge. Both parties had the opportunity to see whether relational capital should be further developed. If something went wrong during the interaction process, the relationship could stop at the early phase of cooperation. Basing’s entrepreneur had a similar opinion on this issue:

“I think the only thing the entrepreneur could do is to increase the ‘match’ or ‘fit’ of the new venture with venture capital investment portfolio. Relationship, perhaps, is important to increase the match, because the more you interact with VCs, the better you understand the investment policies of that VC firm and you know how to cater your firm for venture capital investment. In the same vein, the more VCs know the capability of the team and the key competitive advantage by accurate flow of information, the more likely they will be to invest in the firm. That was what we did in practice to get venture capital.” (Entrepreneur – Basing)

The comments of Basing’s entrepreneur concluded that the more you interact with VCs, the more the VCs will trust the startup team, understand the international business strategy, and establish shared goals toward future growth that, in turn, increase the likelihood of obtaining funding. In general, interaction affects the formation and development of relational capital in the venture capital decision-making process.

Interaction can also be associated with outcomes of value-added services or value appropriation for internationalization in the post-investment stage as shown
by the empirical data. A positive example occurs in Sending’s case, in which the
VCs took a hands-on approach and often organized face-to-face interactions:

“Especially in the very beginning of the company, the investors helped a lot,
like establishing the strategies, like formulating the business, on the R&D
funding, how to organize, and how the business organizes and how it would be
able to differentiate from the others. It was very like a workshop kind of
cooperation, and we met quite regularly and we had some issues to discuss and
checked out.” (Entrepreneur – Sending)

The frequent interaction added more value to the INV, enabling the company to
make quick decisions to react to change. However, Viewing was in a different
situation from Sending. The entrepreneurs were the main decision-makers for
Viewing, although venture capital accounted for over 50% of the shares of the
company after the third round of investment. The VCs trusted Viewing’s
entrepreneurs’ abilities, relied on their knowledge regarding products, and trusted
their vision, which was based on industry trends. Post-investment interaction
between Viewing and the VCs occurred only through regular board meetings, but
both parties were happy with the hands-off approach of the VC firm. In short,
frequency and method of interaction between VC firms and INVs was case-
dependent for each INV.

VCs’ perspective

The U.S. venture capitalist for Placing maintained interaction with the entrepreneur
through phone calls, emails, and face-to-face meetings. Due to the long distance
between them, the venture capitalist made full use of telecommunications for
contacting the entrepreneur.

“Firstly, we had a Skype conference call, a few of them, and sent company
presentations by email, and then had a video conference all again. Then, they
invited the venture capitalist visited the company, in Finland. Afterwards, we
met all potential VC firms in Helsinki, spent a half a day in conversation, and
had a dinner.” (Venture capitalist – Placing)
The U.S. VC firm also established a cooperative relationship with other venture partners from other countries through phone calls, traveling to other countries, and establishing investment networks for interesting investment cases:

“I have a cellphone, and I talk to my partners just like you that I have a conversation with. I regularly, I mean, meet my partners. You don’t need to be the same physical locations. You can effectively conduct the business internationally... We travel around the world for proposals, e.g., to find a promising investment like Nokia, and we have a team in EU, Asian, South America. We used to conducting the business in a global scale, communication and traveling a must.” (Venture capitalist – Placing)

Sending’s venture capitalist believed that most of the startups were investment-ready, but investment readiness is not enough, and it only serves as a prerequisite to approach VC firms. The critical issue at the pre-investment stage, according to him, is to establish a relationship with the INV:

“The more entrepreneurial firms interact with us, the more likely the firms will get invested, because we know you (your team), your company’s product and market offerings, needs and wishes, so that VCs know how to guide and help you after the investment.” (Venture capitalist – Sending)

Similarly, Sending’s venture capitalist used interaction as an information exchange channel to learn from prospective INVs. The venture capitalist learned about INVs’ products, team, and capability for internationalization from interactions, giving him a better view of the overall quality of the INV before making an investment decision. He also continued his emphasis on the importance of interaction during post-investment activities:

“Building the relationship with potential startups is even more critical for us, and continuous development of the relationship is needed to monitor distinct business operations.” (Venture capitalist – Sending)

His comment indicates that he was able to obtain more information about the INV’s current situation through interaction with the entrepreneur during post-investment activity. Indeed, interaction could become an informal information channel through which the venture capitalist could understand more about the INV at the operational
level. Interaction can be an informal way to access information for monitoring purposes.

**Summary**

Regarding the benefits of interaction, both entrepreneurs and VCs hold similar opinions. They all believe interaction is important for increasing trust and building the relationship. Interaction occurs at the personal level and at the business level. On a personal level, interaction occurs mainly through social activities such as dinner, company visits, and phone calls through which they can create goodwill. On the business level, entrepreneurs make presentations, initiate dialog with VC firms, and have discussions to understand VC firms’ investment policies.

VCs consider interaction as a way to obtain information about the INV in the pre-investment stage, such as its products, technology, and foreign markets. Through interaction in post-investment activities, VCs may learn more about the INV beyond what is formally reported, thus interaction can be considered an informal way of monitoring INVs. In general, interaction increases the chance of open communication, facilitates information exchange, and increases the level of trust between INVs and VC firms.

### 5.3.4 Controlling for liabilities and costs

Liabilities related to internationalization are a major concern for INVs and VC firms. As discussed in section 5.3.1, “New venture internationalization,” the INVs often experienced a lack of funding and resources for internationalization. At the same time, VCs considered the costs and tasks involved with internationalization that the small INV teams could not afford. The ability of the entrepreneur and VCs to offset risks and cope with liabilities related to internationalization was important for relational capital formation.

**Entrepreneurs’ perspectives**

The ability to control liabilities and costs associated with new venture internationalization is a major criterion of VC firms in the deal-evaluation process. Case entrepreneurs understood what VCs were looking for:
“If internationalization is concerned, the most important criteria they looked at were the team, its expertise, international experience, willingness for collaboration, and commitment. Products and business ideas together are considered as innovation, and the VCs expected to see how the innovation fits to the international markets and how we can reach the international markets. They expected the new venture to have international markets and be reactive to the market change.” (Entrepreneur – Basing)

This comment reflects the fact that Basing’s entrepreneur was not a purely technology-oriented entrepreneur, as he understood one criterion that VCs looked for was the ability to launch products into foreign markets. Additionally, he understood that intellectual property (IPR) in Finland was the source of sustainable competitive advantage, and he was fully committed to the new venture rather than doing many other activities at the same time.

**VCs’ perspective**

As shown in the case companies, the entrepreneur often acted as CEO, and the entrepreneurial team members maintained various managerial positions in the INV. Their decisions directly influenced internationalization performance. VCs would assess the entrepreneur’s and entrepreneurial team’s abilities in terms of international experience, domestic and foreign networks, and ability to execute the internationalization plan. A venture capitalist explained the evaluation criteria for INVs:

“You must always need to have a market. It may not be today but in the future you need a market. Then, you look at another factor. You should look at underlying technology, what makes you unique. You look at the team, and I would say the team is very important, because there are the ones that executing, you need to make sure that you have a good team. You may have a good technology, but the products cannot be sold by themselves; it is sold by those people.” (Venture capitalist – Placing)

“The overwhelming response from VCs has been that they do not have business expertise in order to get the product involved. The question pops up by VCs is, ‘Who will buy them (products)?’” (Advisor – Placing)
The advisor had worked with Finnish companies trying to get venture capital and had attended venture capital meetings with them. She realized the real problem identified by VC firms was not related to technology or internationalization, but a concern on the part of the VCs about the entrepreneur’s lack of business competence. Assessing the entrepreneur’s or entrepreneurial team’s ability to internationalize is one of the most important components of evaluation. 

*Basing’s* entrepreneur explained the composition of his team for the VC firm’s evaluation:

“I acted as CEO for Basing, and the management team also included the former two top-level managers from Nokia, and one former manager who had over 20 years of work experience in the U.S. in the venture capital financing sector.” (Entrepreneur – Basing)

As *Basing* only got venture capital from Finland, the entrepreneur and the entrepreneurial team believed their knowledge of the U.S. market and the technology was better than that of their Finnish investors. Based on the U.S. experience and networks that the key employees obtained in their previous work experience, *Basing* was able to mitigate the risks and costs associated with the liabilities of newness and inexperience. This was also the reason why the entrepreneur chose the U.S. as the first market to enter.

*Viewing* was in a similar situation to *Basing*. *Viewing*’s entrepreneur had extensive work experience and industry knowledge from serving as CEO of one of Nokia’s subcontractors for years. The company already had built an extensive network and clearly identified the potential international industry players to approach. A clear vision of the wireless industry’s future, together with a deal signed with a Japanese customer, allowed *Viewing* to easily obtain venture capital:

“For the first round of venture capital investment . . . actually they are approaching us.” (Entrepreneur – Viewing)

The ability of the entrepreneurs to achieve new venture internationalization was important for passing the deal evaluation stage with VCs, and in one case even compelled a VC firm to knock on the door of the INV. However, not all of the case INVs had an internationally experienced entrepreneur or sufficient resources to hire an experienced person in the startup phase. As the U.S. venture capitalist for *Placing* commented:
"You need to look at Placing in Oulu is really a R&D team, it is all about technical individuals, we have a multiple of PhDs and masters. We can see is all research group, so we have established Silicon Valley, a commercial team. It is the team that will conduct the commercial businesses. So we have hired a capable person to handle this. Placing has an office in Silicon Valley, and so we are focusing on commercial relationships with customers." (Venture capitalist – Placing)

The venture capitalist thought the biggest challenge Placing faced was not related to technology or market potential, but rather the purely R&D-oriented team and their questionable ability to commercialize the products. Although Placing’s entrepreneur was not an international business-oriented person, Placing still received investment from the VC firm. This might be interpreted to indicate that if a business is promising, a lack of knowledge about internationalization does not preclude obtaining venture capital.

In fact, investing in an INV managed by an internationally inexperienced entrepreneur or team depended indeed on the capability and resources of the VC firm to build up the commercial business. In the case of Placing, an experienced staff would be recruited through the U.S. VC firm for product commercialization and internationalization, especially in terms of the U.S. market. Accepting the personnel recruited by the VC firm required the entrepreneur’s cooperation and understanding. The action that Placing’s VC firm took aligns with this comment by a venture capitalist interviewed in Italy:

“If the original entrepreneur does not have an international mindset, some other experienced guy can, at any moment, assist him. Understanding the entrepreneurial collaborative attitudes towards VCs is quite important, and it takes time to learn from each other.” (Venture capitalist – Italy)

Clearly, the resources of the VC firm are not the only reason for allocating the investment. As a trusted investment partner recommended Placing to this U.S. venture capitalist, referral played a critical role in the process of VC decision-making. In the case of Sending, an undergraduate without any international network or work experience established the company and received venture funding based on a referral. The venture capitalist explained the reason for the decision to fund:
“Sending team is very smart and they learn fast. We help with them finding a right person joining the team. We recruited the people. Obvious as I said, they actively think to approach customers, and they have to hire a person to do that.” (Venture capitalist – Sending)

Because Sending was previously backed by angel investors, it led the company in a clear direction and offered the founding team insight into using a customer-oriented approach. Sending’s entrepreneur appreciated the coaching role of the angel investors and how they scaled up Sending’s business:

“Especially in the very beginning of the company, the investors helped a lot, like establishing the strategies, like formulating the business, on the R&D funding, how to organize, and how the business organizes and how it would be able to differentiate from the others. It was very like a workshop kind of cooperation.” (Entrepreneur – Sending)

Due to the angel investors’ involvement, the team gradually became professional and customer-oriented, which aligned with the thinking of VC firms:

“We often discuss with angels, not just with us, between us, with angels, with teams also. There might be a little bit of external valuation coming. We end up doing syndication quite often as we are investing in very early stage of company, where might be angel involved.” (Venture capitalist – Sending)

Sending’s case indicates that external investors or parties who can help INVs validate their international business plans and increase the team’s capabilities to execute the plan increases the likelihood of raising venture capital, especially for ventures funded by internationally inexperienced entrepreneurs. Sending’s entrepreneur clearly understood the weakness of inexperienced technology entrepreneurs and difficulties in foreign markets. Therefore, the entrepreneur was eager to gain international experience and relationships with network-rich VC firms that could add extra value to their internationalization process:

“That is one option that we could have funding from venture capitalist who know the market and culture . . . If investors only bring money, not competence, we are not interested in. Business knowledge of VC firm direct to the market was the remarkable side.” (Entrepreneur – Sending)
Sending’s entrepreneur’s comment touches on the key point of finding “match” and “fit” between INV and VC firm. He clearly positioned the entrepreneurial team as inexperienced and network-poor; therefore he was open to looking for VC firms that were able to bring business competence to executing their internationalization plan. His consideration aligns with VC firms’ general preference for the kind of INVs they like to invest in:

“We are willing to invest in industries and companies they are more familiar with and in which we can add more value in terms of our personal network of contacts that can easily open new markets.” (Venture capitalist – Italy)

Overall, the entrepreneurial team’s willingness to learn, the assistance from angel investors, and clear demands from the VC firm made it possible for Sending to find the appropriate VC firms in the Finnish local market.

Summary

Consideration of liabilities and risks occurs mainly from the VCs’ perspective. They need to control the risks and uncertainty of internationalization before making any investment decisions. The decision to invest in new venture internationalization depends largely on the entrepreneur and entrepreneurial team and their abilities to offset the liabilities and risks associated with new venture internationalization.

The data shows the factors that affect the decision to begin forming relational capital: first, determining the entrepreneur’s ability to achieve internationalization in a negotiation process is very important and directly influences the possibility of forming a relationship with a VC firm. This ability can be demonstrated by evidence of established networks by the entrepreneur or other key members of the INV, as well as track records of extensive international experience in related industries. Second, if the technology is promising and shows definite market potential, VC firms will evaluate their own ability to recruit someone who can assist in internationalization and execute in the target markets, or whether the syndication partner will have the ability to cope with internationalization-related liabilities and risks. Third, external investors and organizations such as angels and public support companies can enhance the business expertise of entrepreneurs. This provides a positive signal to VCs, especially when the relational capital of the INVs and external investors continues after venture capital becomes involved.
5.3.5 Valuation of the INV

Valuation of an INV determines how much equity is retained by the entrepreneur and how much is shared with the investor; it also serves as a basis for fundraising in the following round. Valuation is one of the key issues to be negotiated in the deal structuring phase of the venture capital decision-making process, according to venture capital literature. The empirical data shows that valuation is actually one of the most important issues that determines the relational capital formation between the INV and VC firm. Often, disagreements occur regarding valuation and control of the INV.

Entrepreneurs’ perspectives

The empirical data indicate that entrepreneurs from case companies often expressed their strong opinions about valuation and willingness to relinquish control of the INV. As valuation of an INV is internal rather than public information, entrepreneurs mainly described valuation in terms of control, and explained what kind of impact a new ownership structure would have brought to formation of relational capital. They also discussed the impact on the feelings of the entrepreneurs and the team toward utilization of relational capital. The entrepreneur from *Chaining* was the most vocal among the entrepreneurs who opposed VCs’ influence on the INV’s future:

“For early-stage investors, we understood they use low price for more shares, because it’s high risk . . . But, if you keep 20% for venture capital, of course, they get 20%, but you need to sign the shareholders agreement, which keeps much more, almost full power of the company from 20% . . . I want to keep control of the company, and we want to make the decisions and influences on the companies.” (Entrepreneur – *Chaining*)

The entrepreneur of *Chaining* was willing to make decisions by himself and build up international business for *Chaining* without external guidance. As the entrepreneur was not in favor of private venture capital as a financial instrument, he instead obtained corporate venture capital from the Finnish government. When asked about his reasoning, he explained:
“Yes, a Finnish venture capital organization was involved, but it is the publicly owned and they have their own rules and no exit plan. It was good, and it is the seed-phase finance they gave. And their target was also to exit from the company as soon as possible. They take the money out from the company, but they don’t control the company. It is good for us.” (Entrepreneur – Chaining)

His comments indicate that the venture capital from the Finnish government was more like a loan, merely providing funding for Chaining. Although the government organization held the ownership of Chaining, they were not strategically involved in decision-making, nor did they push for an exit, as if the money could be paid back. The entrepreneur’s comment also reflects that he was not opposed to the use of venture capital as a financial instrument, only to its source.

The biggest concern for him was who would control and make decisions for the INV after a VC firm became involved. If decision power remained with the entrepreneur, as in the governmental venture capital situation, he was willing to accept the terms and conditions set. He wanted to raise venture capital; otherwise, he would not have invested so much time and effort in the initial phase of approaching and negotiating with VC firms. The problem in his case was the negotiation of power with the VC firm. Additionally, Chaining’s entrepreneur understood that he would need to adapt the company’s reporting system based on the VC firm’s guidelines, and he was not willing to make the necessary changes:

“We do things and we report things that we need to run the companies. We are quite lucky we do not have these venture capital companies, and we do not need to report those kinds of things for them for what they need. We report only for our own needs.” (Entrepreneur – Chaining)

Because he was not able to fully control and foresee the future of Chaining, nor willing to be monitored and to report to the VC firm, the investment agreement was not signed in the deal-structuring phase.

Basing’s entrepreneur acted differently from Chaining’s entrepreneur. While Chaining’s entrepreneur understood the VC firms’ requirements, but he was unwilling to cooperate, Basing’s entrepreneur both understood and was willing to cooperate with VC firms’ reporting requirements and made adaptations accordingly:

“The entrepreneur should stay in control, because we know the business better than outsiders, but I would like to emphasize the cooperative nature of the
entrepreneur and venture capital relationship. We are willing to adapt, e.g., based on venture capital evaluation criteria, reporting system requirements or by recruiting new staff through VC firm’s networks and have frequent communication.” (Entrepreneur – Basing)

In reality, Basing’s entrepreneur did not want to completely lose control of the venture, but he tried to adapt and compromise based on the VC firm’s requirements, which created a feeling of being monitored and controlled by the VC firm.

Viewing was in rather different situation. Viewing’s VC firms even did not monitor Viewing’s business operations. The entrepreneur mentioned that the Finnish VCs were not as experienced as the entrepreneurs in terms of the industry and working with foreign customers, and they gave almost all decision-making rights to the entrepreneurs. Controlling the INV was not a focal point of relational capital in Viewing’s case.

The actual problem Viewing encountered in the third round of investment was the dilution of the entrepreneur’s and key employees’ shares. The change of ownership structure dramatically changed the people’s feelings when their shares were diluted to 14%. However, due to lack of funding to get out of the industry’s downturn, the entrepreneurs had no choice but to take as much venture capital as possible to keep Viewing afloat. As a result, the ownership of the VC firm increased up to 50%, which left only a small amount of shares for the entrepreneur and key employees. The entrepreneur described the change of attitude toward relational capital between the INV and the VC firm:

“It changed actually the atmosphere or attitude that we don’t own the company anymore, like it was used to be . . . The dilution was too hard until 14%. Even the VCs didn’t understand how big influences (it was) in people’s mind. It (the share held by entrepreneurs and key staff) was so low, and actually they should be carefully . . . From their perspective, it was good time for VC firms because it was the hopeless time for hardware wireless businesses. They didn’t recognize that (we felt) VCs were not in the same boat with entrepreneur and employees, and they were on another side of the negotiation table.” (Entrepreneur – Viewing)

The third round of investment resulted in Viewing’s entrepreneurial team feeling as if they no longer owned the company and were just employees of Viewing. Their care, passion and enthusiasm for the future of the company disappeared. The
entrepreneur explained that the VC firm did not offer any optional payback program through which the entrepreneurs could buy back their shares. The entrepreneur felt they were unfairly treated by valuation, which decreased their shares only to 14%:

“It’s the question of valuation of the company, and they couldn’t value the company more, even by offering optional program.” (Entrepreneur – Viewing)

The comments made by Viewing’s entrepreneur suggest how VCs should be aware of the effect of valuation of the company and the percentage of entrepreneurs’ shares. Otherwise, entrepreneurs can conclude they are being unfairly treated, which decreases the motivation of the entrepreneurs to contribute to the INV and destroys relational capital. Similarly, Basing’s entrepreneur also suffered from low morale after being unfairly treated in terms of valuation:

“I discovered that the amount of VC investment would be deducted from the valuation. It came to me as a surprise, while VCs took that as granted. I felt disappointed about it.” (Entrepreneur – Basing)

Basing’s entrepreneur guessed that the VC firm purposely changed negotiation dates with short notice, which made it impossible for the entrepreneur to prepare for the meeting and left insufficient time for the INV’s lawyers to check the terms and conditions. When he realized that all money Basing had borrowed was deducted from valuation, he was shocked. He tried to suppress his feelings of being unfairly treated, admitting:

“I think that I were able to put aside the bad feelings on what came into actual operations, and cooperation, but it perhaps affected the openness of the communication overall.” (Entrepreneur – Basing)

Viewing’s and Basing’s cases indicate that valuation affects entrepreneurs’ motivation to contribute to the INV and changes the psychological feelings related to ownership of the INV. The change of attitude might directly impact the development and utilization of relational capital, or even result in relational capital failure and, as in Basing’s case, replacement of the entrepreneur as CEO.

Placing and Sending were actually in good financial situations and were able to attract many investors. Therefore, discussing valuation was not as tough as in Viewing’s case for the second and third rounds, nor as in Basing’s case, which
depended on the VC firm for financial capital. Therefore, Placing’s entrepreneur was able to achieve higher valuation so that he did not lose control of the company. He described his strategy as follows:

“I knew our valuation was high, since we did not want to give too much shares to them, like 20%–30%. We insisted on our decision on valuation (negotiation with Asian venture capitalist) . . . I like more investors than just one, so you can keep equal shares to all the investors. No single investor will have a strong decision power in post-investment stage.” (Entrepreneur – Placing)

“We are in good financial situation and do not rely on VC firm’s capital. We want the VC firm that can bring business competence.” (Entrepreneur – Sending)

In other words, if the INV’s financial situation was good, the INV did not depend on venture capital to expand, and the entrepreneur could have a better strategy to reserve control rights of the company.

**VCs’ perspective**

The ability to control the INV was also a concern of VC firms. The anonymous venture capitalist interviewed in Italy explained the importance of control in terms of INVs’ success:

“We should learn more about new venture teams and their capabilities for internationalization, and whether we are able to exercise control after investment.” (Venture capitalist – Italy)

VCs did not mention control issues separately as a criterion in their decision-making process. The entrepreneur’s willingness to collaborate might have demonstrated willingness to be controlled, because entrepreneurs understood monitoring was one of the most important activities in the post-investment stage. The VCs interviewed mainly shared their viewpoints on INV valuation, which turned out to be very different from entrepreneurs’ thinking.

Sending’s venture capitalist said that the first negotiation round with Sending’s entrepreneur did not go through. The venture capitalist explained that Sending’s financial situation was in such good condition that they were not able to agree on
valuation. However, in the second round negotiations, together with another VC firm, the investment agreement was signed. The venture capitalist thought the second round was fairly easy, due to investment syndication:

“It is important to figure out what is the right value, which is fair, and in any trade, there are a lot of investors like we are: pretty tough negotiators when we feel the valuation is too high. So I can still not really say that because cooperation increases knowledge, that enables us to price the company right, either right or might not be for entrepreneurs in terms of valuation.” (Venture capitalist – Sending)

Before the VC had committed to the INV, the VCs held the information advantage over the entrepreneurs. This might raise a question about whether entrepreneurs should disclose information, because revealing information could demonstrate a willingness to build relational capital which in turn could be exploited by VCs during negotiations. As a consequence, when VCs held the information advantage, the INV was priced lower than it should be. In addition, the venture capitalist was cautious about valuing the INV because it would have an impact on the next round of financing:

“It is not just because of valuation, because if the value is too high when we invest, and valuation in the following round will be lower, and we will feel we get scared off, and that could not be able to make a good starting point for the company, and work with company further. So, it is not easy to define the company and the value just with the money.” (Venture capitalist – Sending)

Pricing of the INVs was also based on whether other VC firms joined in the next round of investment. If the valuation were much lower in the second round, the VC firm’s situation would be more tenuous. As such, VC firms had to consider not only the interests of the INVs, but also their own interests in the following round of investment, as well as the potential impact on return on investment.

Summary

The empirical data provided rich information concerning valuation’s potential impact on the formation, development, and utilization of relational capital for new venture internationalization. In particular, the voices of the entrepreneurs were
extremely strong regarding what can negatively affect relational capital with VC firms. From the entrepreneurs’ perspective, valuation and control of INVs determines relational capital continuity and quality. Whether the entrepreneur feels fairly treated in terms of valuation relates directly to the quality of relational capital during the post-investment stage, in which joint decisions need to be made.

In extreme cases, the entrepreneur may totally abandon venture capital as a choice in order to maintain full control of the company, as with Chaining. Most of the case companies’ entrepreneurs suffered from a feeling of losing their ventures, but they tried to adapt, to compromise, and to find the balance of decision-making power that satisfied both parties. Relational capital accumulated through the investment process can facilitate finding the appropriate way to collaborate. The entrepreneurs’ concerns about the possibility of losing control of the INV after the VC firm’s involvement affects relational capital formation.

VCs considered valuation of the INV not only based on the company’s inherent value, but also on projections for the next round of investment. Venture capital might use their information advantage for their own interests, but feelings of being treated unfairly would decrease the offerings from the entrepreneur’s side after investment, as experienced in Basing’s case. Surprisingly, the empirical evidence showed that valuation and control, or the psychological feeling of ownership, was the most important factor that affected the formation and utilization of relational capital for entrepreneurs.

5.4 Exploring the utilization of relational capital

This subchapter analyzes the empirical data related to utilization of relational capital between INVs and VC firms for the purpose of new venture internationalization. A series of factors determines the possibility of forming relational capital through pre-investment interaction and its level of quality. After the venture capital investment agreement has been signed, the focus switches from building to using relational capital during post-investment activities. Some case companies worked well with VCs and achieved value appropriation through relational capital utilization, while others encountered relational problems that led to venture failure. The subsections 5.4.1 and 5.4.2 discuss these issues in detail.
5.4.1 Alignment between INV and VC firm

The alignment of an INV’s and VC firm’s interests and goals is a crucial factor for venture success, and the importance of strategic goal alignment to the success of a VC-backed venture has been widely acknowledged. Yet, goal incongruence often occurs in practice, as described by the advisor:

“When they are in control, they had communication issues. Because the core group were engineer, the entrepreneur is very much engineer, and he does not understand, and has abilities for business, where the investors usually look for growth. I think it is very difficult.” (Advisor – Placing)

“Alignment, remember that investors and founders of the company do not always aligned. They have different visions where the company should go, different markets. If you are not completely aligned, you will meet difficulties.” (Venture capitalist – Placing)

These comments from Placing’s advisor and venture capitalist point out the conflicting goals and interests between Placing and the U.S. investors related to scaling up the business. The entrepreneur was following the ordinary Finnish INV procedures, putting more emphasis on developing products. However, the U.S. investors were especially seeking growth through foreign market orientation.

Goal alignment may occur during the relational capital building process, during which the INV and VC firms continually consider their own goals and shared interests.

Entrepreneurs’ perspective

The entrepreneur for Placing realized the importance of alignment with the VC firm during post-investment interactions, especially when conflict occurred. He feels they encountered only one conflict. According to him, the best way to deal with it was open discussion and being straightforward and decisive. The conflict should be handled at the cognitive level, assessing how the different proposals would affect the company and serve the best interests of all involved, based on the facts. However, he also used the relationship he formed with all investors, as follows:
“As a founder, if you have a good relationship with shareholders and other, you can use that to leverage to resolve the conflict. The conflict is related to one of the investors, you can use good relationship with other investors; you can use group pressure to resolve the conflict.” (Entrepreneur – Placing)

This entrepreneur was smart in the way that he utilized the relational capital he had built with different investors during the pre-investment stage to resolve the conflict based on the concrete facts of the situation.

Having relationships with VC firms is also a learning process for entrepreneurs, as Placing’s venture capitalist described:

“Those individuals do not always like Steve Jobs . . . He learnt from there what to do. Please remember he was fired by the board, he learnt, and back, learnt market. Again it is a tremendous learning. Sometimes, you lost this company [involving] bankruptcy and failures, but through that very difficult time, [it is] a high growth.” (Venture capitalist – Placing)

However, this comment was not related to what happened to Placing. It represents the venture capitalist’s thinking in general terms about the worst-case scenario of venture failure from a poor relationship between an INV and VC firm. Basing experienced venture failure due to mistrust and a poor relationship. The entrepreneur was dismissed as CEO and replaced by a candidate recommended by the board. Without the entrepreneur’s passion and knowledge, Basing ended up going out of business. Basing was the first VC-backed INV founded by the entrepreneur that did not succeed. He shared his feelings about it well after the fact:

“I am glad that I had a chance to meet the people I met (VCs) and learn from them.” (Entrepreneur – Basing)

Basing’s entrepreneur considered the experience a process of learning how to work with a VC firm. “Learning by doing” is a good practice for the entrepreneur who has formed and dealt with relationships with VCs. The experience can be further applied to other VC investors in the following round, or even to later ventures.

Placing’s entrepreneur, while also CEO of the INV, understood that he was not the professional CEO the VCs expected. He quickly learned how to change from the role of academic professor to become a good CEO. He realized that only when
the relationship with the VCs was pleasant, and the performance of Placing was good, was he able to continue as CEO and to control the company:

“Obviously, one like matter is when I am as a founder of the company, I haven’t been a CEO before, I came from academia, and I didn’t understand the business at all, so they have concerns that should someone in some point should be a professional CEO.” (Entrepreneur – Placing)

He reacted to this point with self-evaluation as well as giving the feeling to the VCs emphasizing the role of founder and his vision in success of Placing:

“Now, the trend today is really to support one of the founders to be CEO. Of course, depends always personality: the person should be grown as a person and to be CEO. Someone who understand the vision and create the vision, and understand the whole company, the team, how team got together. If you bring a professional CEO who doesn’t have vision, nothing will happen, definitely. In later round, some investors may not care who will be the CEO, and bring professional coming in, maybe some of their guy, but I don’t want this happen.” (Entrepreneur – Placing)

The entrepreneur positioned himself well in Placing and understood that he might be replaced through the board, so he tried to maintain a good relationship with the VCs and show his capability for international business. He also showed willingness to collaborate and carefully reported the progress of the INV to shareholders, according to different situations:

“We collaborate with Asian investor at the technology level, and they have appointed a board member. It depends on VC firms; some VCs may be quiet, and weekly dialog is enough. For some of VC firms in U.S., I should often travel there and meet them face to face.” (Entrepreneur – Placing)

VCs’ perspective

The relational capital accumulated in the formation process increases the trust between INV and VC firm. This increased trust helps the entrepreneur and VCs avoid misunderstanding and stay focused on important issues, as described by Sending’s venture capitalist:
“Good relationship gives more flexibility for companies and for us. It means we have to work less and we can focus on really important stuff. The time will be better spent for both of us, which makes the company more effective and reactive.” (Venture capitalist – Sending)

Sending’s VCs commented goal alignment has been benefited from relational capital. VCs exercise monitoring through the INV’s board of directors, who guide the direction of the company:

“It is a collection of the people, and you need to play another rules. I would tell you this that investors on the board make decision, and we have removed the founders. It is not a pleasant situation, but we have to remove this person from the company. We have to do the best interest of the company.” (Venture capitalist – Placing)

The board serves an important role in guiding INVs, therefore it is important to take care of the relationship with all investors and find the best approach to working together. It is case-dependent whether the board should use a hands-on or hands-off approach. Only when mutual understanding is increased through interaction and open communication can the appropriate working approach be found.

In the case INVs, the U.S. investors, including angels and VCs, were focused on a hands-on approach to acquiring customers and searching for possible syndication investors. The entrepreneurs considered them mentors because they had seen so many startups, and it was helpful to involve them in shaping strategies. However, with the Asian investors, the hands-off approach took the form of daily communication via email or other electronic means for monitoring the amount of usage of the technology. The Asian investors were not involved on a strategy level, because they were investors interested in the technology only, rather than focusing on profit.

Sending was in a rather similar situation. In the seed phase, a hands-on approach was efficient for bringing in the management know-how of investors. When entering the startup phase, the entrepreneurial team was learning fast and had already achieved milestones for acquiring customers. Sending demanded more flexibility in making decisions, at which point the approach shifted to hands-off.

Viewing’s team was experienced, and their investors did not have the competency to offer more value-added services through their network resources.
Therefore, the VC firm took a hands-off approach and put trust in the management team to make strategic decisions.

In Basing’s case, it was somewhat different. The entrepreneur appreciated the hands-on approach to developing the U.S. market. However, the relationship collapsed due to inadequate communication and trust in him as CEO, in addition to doubts the entrepreneur had about the VCs’ decisions. The failure of relational capital in Basing’s case made for misaligned goals and strategies during post-investment activities, leading to venture failure.

**Summary**

To align the goals and strategies of entrepreneurs and VCs, open communication should be achieved through the relational capital building process, during which information is exchanged and the strengths of both parties are acknowledged. The entrepreneur should understand well his role of CEO and be able to demonstrate his ability to make decisions in an uncertain environment. The entrepreneur should show his willingness to cooperate and to be monitored, for which utilizing relational capital is an important strategy. At the same time, the entrepreneur must maintain his own strengths and decision-making power. When it comes time to resolve conflicts, the discussion should be kept on the cognitive level and should be based on facts without turning it to be an affective conflict, leading to mistrust that continues through later stages. VCs should be entrepreneur-friendly. They should acknowledge their vision, decisions, and ability to foresee the future of the INV, especially when the INV is proceeding well. The VC firm should offer flexibility to entrepreneurs in operating in uncertain environments, and they should be constructive in helping with development. Finally, the exchange of information during the relational capital building process can facilitate the finding of an appropriate approach to keep the business and relationship going in a positive direction. Utilization of relational capital is important in aligning goals and strategies between INVs and VC firms.

**5.4.2 Value appropriation from VC firm’s network and resources**

In the venture capital context, value appropriation refers to the amount and quality of value created for the INVs and VC firms engaged in collaboration. Value generation is seen as both a product of properly formed relational capital and a
driver for strengthened collaboration. Value appropriation is mainly from the perspective of entrepreneurs, as they are the receivers of the value-added services.

Placing’s entrepreneur was satisfied with all of the investors involved in Placing. He elaborated that the U.S. investors offered great help to develop that market, and the Asian VC investor greatly helped Placing develop the Asian market. He claims that maintaining a good relationship with all shareholders is extremely important, because it creates a good image for other potential customers and investors:

“Asian investor is a great commercial reference. Everybody is looking for references when talking about startups and technology . . . Actually, our customers and potential investors actually met Asian investor and arranged face-to-face meeting in order to understand how the technology works and have they been happy with it.” (Entrepreneur – Placing)

In terms of developing markets, he further elaborated:

“Asia is a large market. Our Asian investor was No. 1 in Asia in the field. It makes us easier to acquire new Asian customers. They also have influence in other Asian countries, particularly in Japan and South Korea.” (Entrepreneur – Placing)

These comments explain that the Asian investor had great signaling effects only in the Asian market, where having a good relationship with the investors could attract more customers and investors to Placing. Relational capital was important, as the customers and investors often talked directly to the Asian investors. If the relationship had been poor, the Asian investors might not have recommended Placing. Placing’s entrepreneur considered the Asian investors as interested in the technology rather than profit. In terms of developing the market, the Asian investors were not deeply involved in the strategy. The level of cooperation was at a technological level.

“Asian investor is more strategic investor interested in technology, compared to U.S. VCs, who are interested in revenue.” (Entrepreneur – Placing)

He continued his remarks by reflecting on the U.S. investor teams, including the angels and VCs involved in the company, as well as the Finnish VC firm involved:
“I don’t think angel investors have increased the valuation of the company. Angels and investors from Finland do not increase the value of the company, because they are not well-known individuals. Of course, they have some connections to help us acquire customers, contact the other investors . . . they look like our team members.” (Entrepreneur – Placing)

His thinking was rather different from the advisor in terms of whether the U.S. angel investors increased the valuation of Placing. His definition of increasing valuation is dependent on the financial calculations of the INV. The entrepreneur did not think the U.S. angel investors had signaling effects for attracting VC firms to Placing. The advisor approached the question from another angle of understanding valuation, believing that angel investors as referrals attracted customers and brought business competence and experience for the U.S. market, which increased the actual value or power of the INV when negotiating with VC firms over valuation.

Sending received venture capital for entering the U.S. market and worked with the VCs for less than a year. The experience Sending had with its VC firm met the entrepreneur’s expectations:

“It was like a very close cooperation, and later on when the company becomes mature, the equity investors are not deeply involved in our business. It is then more like mental spring or such changing ideas on a general level. It does not concentrate on the special issue of the company” (Entrepreneur – Sending)

Viewing’s entrepreneur explained that the Finnish VCs were not able to help the INV approach customers due to their limited foreign investment experience and the size of their fund:

“Finnish VC firm was very small compared with U.S. and had never ever invested abroad. They did not have any foreign contacts and international business experience. Like the bank in Finland, compared the bank, e.g., in Asia, here is a huge differences in terms of size; it’s the same in VC firm.” (Entrepreneur – Viewing)

He elaborated that the Finnish VCs gave flexibility to the entrepreneur to make his own decisions, and they did not require additional reporting work or increase the
bureaucracy for Viewing. He appreciated that the investors were patient during the industry downturn, continuing to support Viewing with capital and positive morale without pushing to exit.Exiting at that point would have meant selling Viewing for a bargain price, because after the third round of financing, the main shares were held by the VC firms. This good relationship kept the business going. In the same vein, the Placing entrepreneur explained:

“Usually, VCs are entrepreneur-friendly. However, if the company does not performing, they will not be friendly anymore. It is understandable because it’s their job to take care of their money invested.” (Entrepreneur – Placing)

However, due to the amount of relational capital, fortunately this was not the case for Viewing. The VC firm shared the INV’s pain and offered understanding, based on their trust in the entrepreneurial team and belief in their ultimate success after the challenging period was over. Decision-making flexibility granted to the entrepreneur by VCs was also evident in Placing’s case:

“The good relationship increase trust of VCs on management team and their vision on the company: therefore, they give much flexibility to us.”
(Entrepreneur – Placing)

Relational capital increases the level of trust, offering greater flexibility to the entrepreneur to operate and make strategic decisions in an uncertain international business environment.

VCs do not conduct their investments alone, but typically have syndication partners. VCs believe syndication partners add value to VC firms:

“I think our co-investors have done a lot of jobs. When syndication occurs, I cannot say it offset risks, but definitely a bit more knowledge and resources involved.” (Venture capitalist – Sending)

Summary

Value appropriated from relational capital is mainly from the entrepreneurs’ perspective. A good relationship with the VC firm can translate to a reference, which is particularly valuable when the VC firm is well-known in the local market. Commercial references have strong signaling effects both to customers and
potential investors. In turn, accumulated relational capital keeps VCs motivated to explore additional markets, provided they have that capability.

Another outcome of relational capital is recruiting talented people through the VC firm’s network into management positions. The track record of the recruited talent adds value to a reference, in addition to bringing in management know-how. This management experience is extremely helpful in scaling up the team and developing international business. Relational capital increases the trust between the entrepreneur and VCs, so that the VCs are comfortable giving the entrepreneur greater flexibility to make decisions. This flexibility keeps the entrepreneur motivated to offer his vision as a founder, in addition to his technological knowledge. Finally, the accumulated relational capital increases the patience of the VC firm and their commitment to the INV, motivating them to offer continuous capital and emotional support. Utilization of relational capital can achieve better financial results and performance for the INV, which secures the return on investment for the VC firm:

“Building relational capital is an important factor, but it is a two-way process: VCs should also build relational capital towards potential entrepreneurs and international new ventures to learn more, and thus mitigate the risks involved with their investment.” (Venture capitalist – Sending)

5.5 Issues emerging from the data

This subchapter discusses the emerging issues that are not identified as constructs in the theory. These issues, grounded in the data, influence the formation and utilization of relational capital between the INV and the VC firm. They also provide new insight on the dyad relationship and shed light on further exploration of the topic.

5.5.1 External environment

Stories of both success and failure of VC-backed ventures that occur in the entrepreneur’s network can potentially shape the view of the entrepreneur regarding venture capital.

This was the case with Chaining’s entrepreneur, who heard sad stories within his network related to involvement with VC firms that shaped his views and
opinions about venture capital. Due to the large cost of organizing an international distributor network, he still tried to make use of venture capital, but with caution:

“I have seen some warning signs for us. There was a company in Oulu, and they had already sold their products quite nice with innovation. It was very much the first phase that the VC firm entered the company, and they signed the shareholders agreement. They gave too much power to VC firm so as to sign up the contract, and then they needed for next round financing, however, VC firm was not be able to invest in more for the company or willing to invest in any more. In addition to that, VC firm was not willing to be flexible with shareholders agreement, so the agreement was so stupid that there is no other investors would like to invest in the company that have already controlled by the VC firm. The company went bankrupt. It’s of course typically the sad case, but it could happen.” (Entrepreneur – Chaining)

Chaining’s entrepreneur further elaborates on his disappointment at not being able to negotiate the investment agreement with any VC firm he approached, because all of the VC firms had to follow a template drafted by the Finnish Venture Capital Association. He was dissatisfied with the unfairness of the negotiations with VC firms. He says that if he had been given a chance to negotiate the terms and conditions, he might have changed his mind. However, he could not negotiate anything with them due to the strict rules:

“It was a couple of years ago, and maybe it has changed. When we had discussed with venture capital companies, all of them say that the shareholders agreement template is similar, and it was made by [the Finnish] venture capital association. It is standardized rule defined by the association, so that we cannot change very much... It is like monopoly that [the Finnish venture capital association] designs the rules that everybody should play with. It’s the same template.” (Entrepreneur – Chaining)

Viewing was in a different situation from Chaining. The wireless industry had just been established, and it was also the time when the VC industry appeared in Finland. Viewing’s entrepreneur described the situation of raising venture capital:

“Actually they (VC firms) were approaching. The VC firms invested in the relevant industry if the company had a sort of drafted business plan. Almost
everyone applied got investment, and it was crazy. Of course, failure cases happened too.” (Entrepreneur – Viewing)

As Viewing’s entrepreneur’s description reflects, besides the relational network of the entrepreneur, the industry’s circumstances also play an important role in attracting venture capital. In the first round of financing, the wireless market was brand new, and investors were eager to invest in the booming industry. VC firms were especially interested in opportunities to invest in any wireless companies with well-drafted business plans.

For Viewing’s first round of financing, it was relatively easy to build a relationship with VC firms. In fact, as the entrepreneur said, the VCs actually approached them. However, the second and third rounds were much more difficult because of the rapid change in the industry. For the second and third rounds, Viewing was not as fortunate as in the first round, due to the Internet industry downturn in the early 2000s. Entrepreneur A from Viewing was devoting almost all his time to working with their current VC firms in addition to identifying new ones to obtain the third round of investment:

“Entrepreneur A was doing that like a full-time job for that. He was just visiting investors, all day job for two years . . . Entrepreneur A was taking care of investors. We took care of strategies, technology, business, and the company . . . Probably entrepreneur A has met 200 VC firms in U.S. and traveled there often. This was also the reason we had office in U.S. There was money located in Silicon Valley; also, our company (had to be) in U.S. We were looking for investors for two years. Hundreds of investors for SMEs had been contacted, but finally it was invested, but by Finnish companies.” (Entrepreneur – Viewing)

Viewing’s strong local network secured the second and third rounds of financing from Finnish VC firms. The reason for not successfully raising venture capital from the U.S. may have been the lack of network connections. Starting from scratch to approach VC firms was a difficult job without any references, especially in a challenging industry environment.

Moreover, the surrounding environment, such as happenings in the local business community and the situation of the industry as a whole, may also affect the motivation, speed and ease of forming a relationship between the INV and VC firm.
5.5.2 Human factors

The empirical data indicate that entrepreneurs behave differently as decision-makers of an INV. Their personal characteristics, experience, and network affected their ways of thinking and working with VCs. Different behaviors were directly related to the building, development, and utilization of relational capital. Some succeeded, and some did not. The following subsections describe the findings in detail.

Entrepreneurs as decision-makers

Chaining’s entrepreneur is the kind of person who prefers having full control of the company and takes direct interest in every detail. The stories of failure of VC-backed firms occurring within the entrepreneur’s network affected his attitude toward venture capital and shaped his views and opinions regarding VC firms. He was also concerned with the exit plan and uncertainty about the INV’s future if the milestones set by the VC firm could not be reached:

“Venture capital companies also have the liquidation preferences, and we didn’t like that. They need the power of the companies, liquidation, and exit plan. It destroys the companies. We are targeting the exit, and if we failed the date, and VC firm can do whatever to the company and take the money, and we don’t know what is going to happen for the company. They take the money, and we say goodbye to the companies.” (Entrepreneur – Chaining)

The comment demonstrates the entrepreneur’s fears of failure and loss of control of the funded venture. His related unwillingness to collaborate hindered the formation of relational capital with VC firms. The reticence may stem from characteristics of the entrepreneur himself, as well as his understanding of the venture capital industry as a whole. He might be the kind of person who prefers full control of the company, and takes interest in every detail. If he did not put forth the minimum effort to adapt his reporting system based on the VC firm’s guidelines, the relationship would not be able to develop further. In addition, he was sentimental, and feared failure and loss of control of the funded venture. As a consequence, Chaining was not able to obtain venture capital for new venture internationalization.
Placing’s entrepreneur believed that his personality fit the role of CEO, and he was sensitive to cultural differences, which helped him manage different relationships:

“Obviously personality builds the trust . . . I haven’t been a CEO before. I came from academia and I didn’t understand the business at all. I am a quick learner and able to act as CEO for the company.” (Entrepreneur – Placing)

Placing’s entrepreneur had an academic background as a professor, and he learned quickly how to become a good CEO. He was open-minded and capable of learning and making changes. His previous academic career increased the credibility of his technology knowledge in the eyes of the VCs. Moreover, his personality gave him a good chance of creating trusting relationships with stakeholders, while his learning ability enabled him to react quickly to changes. He learned especially through communication with VC firms. As a result, he managed to raise venture capital for Placing and kept relationships ongoing with the various investors involved.

Viewing acted as a hardware subcontractor for Nokia for years, which gave the entrepreneurs and key employees extensive industry network connections and experience. When the entrepreneurs decided to transfer their business experience into a new focal area that became Viewing, the reputation is afflicted with the entrepreneur and the image of Viewing. Because wireless was new, and the entrepreneurs already were experienced in it, that the VCs had few disagreements with the entrepreneurs because they lacked personal knowledge of the industry.

Basing’s entrepreneur admitted that he was young and inexperienced, so he was not confident enough to argue or dispute a decision. He realized after the venture’s failure that he was too optimistic about some of the milestones that were related to technology development, market identification and development, and business plan execution, as he describes:

“I were too optimistic about the agreed milestones that affected the valuation of second round, which probably upset the venture capitalist a bit though perhaps wasn’t entirely a surprise; after all, founders typically are overly optimistic.” (Entrepreneur – Basing)

The entrepreneur suspects he was not taken seriously on some occasions, perhaps due to distrust of his expertise by the VCs. For example, his view on advanced open
source models was not taken into account. As a consequence, the decision to replace him as CEO of Basing was made by the board.

**Entrepreneurs’ expectations**

*Chaining*’s entrepreneur expected only sufficient funding from a VC firm to expand international business; he did not anticipate their strategic involvement after investment. However, after several rounds of negotiations with VCs, the entrepreneur realized that the VC firm in any case would monitor the daily operations of *Chaining* and influence decisions through the board. In addition, he learned that they would require him to modify functional systems, such as reporting, after VC allocation. Negotiation results with VC firms did not meet the entrepreneur’s expectations. Therefore, he abandoned the effort to continue developing relational capital with VC firms.

*Viewing*’s entrepreneur actually received venture capital funding only to develop the products and business. The value-added services brought by the VC firms to *Viewing* were not as generous or effective as those brought to *Placing* and *Basing*. Although the VC firms’ network and resources did not help *Viewing*’s internationalization efforts, *Viewing*’s entrepreneur was not disappointed with them:

\[ “Finnish VC firm was very small compared with U.S. and had never ever invested abroad. They did not have any foreign contacts and international business experience. Like the bank in Finland, compared the bank, e.g., in Asia, here is a huge differences in terms of size, it's the same in VC firm.” \]

(Entrepreneur – *Viewing*)

The entrepreneur’s expectation of additional value-added services from the VC firm was rather low, in consideration of their size, international experience and network. *Viewing*’s entrepreneur understood the business and needed only financial investment and moral support from the VC firm. He did not expect help with building international business or finding new customers. Because his expectation was low, he was not disappointed in the VC firm’s lack of contribution to *Viewing*’s internationalization process. The role of the VC firm in the post-investment stage was to serve as a sounding board, thus they took a hands-off approach and did not intrude into the decisions made by the entrepreneurs. Both parties were happy with this arrangement.
5.5.3 Luck or opportunity

According to empirical data, luck or opportunity appears to play a role in forming relational capital with VCs. As described in the previous chapter about external environment, Chaining attempted to raise VC funding under very strict rules governing terms of the agreement. He did not have opportunity to discuss or influence valuation or control rights stated in the term sheet, leading to his decision to give up venture capital as a funding choice.

The first venture capital round for Viewing was rather easy due to the newness of the wireless video communication market. Luck is often with the person or company well-prepared to pursue opportunity. Viewing’s entrepreneur was decisive about changing Viewing from a subcontractor to a business focusing on wireless video technology. The external environment offered many opportunities for Viewing to sign initial contracts with customers, increasing their credibility and negotiation power with VC firms.

However, in future rounds, Viewing was not as lucky as in the first round. Viewing encountered unexpected industry downturn related to the “dot-com bubble,” which gave them trouble obtaining financing. Otherwise, Viewing would be able to rely on revenue-based growth, and the entrepreneur would not be able to give such high percentage of shares to VC firm and lost of control of Viewing. This might be understood to imply that entrepreneurs face greater uncertainty when entering into international environments, particularly in high-technology industries. Luck or opportunity has a tendency to disappear as quickly as it appears.

Placing was the only case INV that raised foreign venture capital. Placing was lucky in the sense that the entrepreneur received a strong referral that connected his company with U.S. angel investors. Through their network, Placing was able to attract a talented person from a U.S. company and to focus on the U.S. market.

Next, a series of activities that took place in the U.S. market gave the entrepreneur a chance to meet an Asian investor who was extremely interested in the technology of Placing. Additionally, the investors from the U.S. had a strong working history as Nokia venture partners, as well as Finnish cultural understanding. They knew the tendencies of Finnish entrepreneurs and their preferred method of building business. Thus, the U.S. investors were not surprised at the Finnish company’s not following the usual U.S. style of doing business.

Through only one connection, Placing was able to connect to various investors. On the other hand, the other case INVs all pursued U.S. opportunities without any
results. Luck became a critical component of Placing’s case, together with a great story to pitch to VCs.

There was some discussion related to timing of raising venture capital, that is, whether INVs should begin approaching VC firms in the first half-year after founding, or wait for a year or two. Basing’s strategy was to start venture capital talks early, compared to competitors. Having the advantage of being the first mover, Basing managed to raise venture capital after tough negotiations. Had Basing waited, the VCs may have expected more in terms of having a ready pool of customers or proven technology. Basing captured the right timing and opportunity to initiate the relationship with the VC firm.

As evidence shows in the case INVs, luck or opportunity plays an important role in forming relational capital with VC firms.

5.6 Cross-case analysis

Cross-case analysis accumulates the case knowledge, then compares and contrasts cases. In so doing, it produces new knowledge. The following subsections examine themes, similarities, and differences across the interviewed cases, seeking understanding of which conditions led to relational capital being formed and utilized.

5.6.1 The role of relational capital in raising foreign venture capital

All of the case companies attempted to raise venture capital from U.S. which is renowned in the venture capital industry and full of success stories. All of them actively networked and traveled frequently to attend pitching events and activities. Basing was not capable of raising U.S. venture capital, although they aimed for it. Neither was Viewing successful in raising U.S. venture capital, although they aimed for it. Basing and Viewing established offices in Silicon Valley. Both Placing and Sending participated in public support organizations’ projects, traveled to the U.S. to pitch VC investors, and participated in other related activities. However, only Placing succeeded in the process.

The entrepreneur of Basing said that he and the entrepreneurial team traveled several times to the U.S. to pitch to investors during the time Basing wanted to enter the U.S. market. The main reason for Basing’s failure in this effort, the entrepreneur surmises, was lack of contacts and references in the U.S. market.
Another reason could be because Basing’s headquarters is located in Finland, making it inconvenient for U.S. investors to control and monitor decisions.

Viewing’s entrepreneur had similar explanations for not receiving investment from U.S. VC firms. According to Viewing’s team, building relational capital with the right firm in a foreign market, especially with VCs, is a critical factor influencing venture capital decisions. Distance between venture and VC firm means missed opportunities for building and developing relational capital, and was the major reason for Viewing’s lack of success at raising U.S. venture capital.

The ability of the VC firm to monitor portfolio firms was another determinant in the venture capital decision-making process. Monitoring is related to the performance of INVs, which affects a VC firm’s return on investment. If a partner was available in Finland, as in Placing’s case, who could help monitor the INV, the possibility of receiving venture capital from overseas was greater.

The only case INV that attracted venture capital from the U.S. was Placing. The primary reason for their success was that the U.S. VC firm itself was an international investment agency, with a Finnish VC firm as a trusted partner. Together with the Finnish VC firm, the U.S. firm decided to become a co-investor in Placing, with monitoring accomplished through cooperation with the Finnish investors. With this U.S. reference, Placing won several times pitching price from venture capital pitching events during 2014 and 2015 (news press). The track record of the U.S. VC firm helped Placing attract more investment possibilities in the U.S. market.

5.6.2 Entrepeneurial power in negotiations with VCs

Earlier analysis in section 5.3.5, “Valuation of the INV;” raised the interesting question regarding entrepreneurial power in negotiation with VCs related to INV valuation. The case INVs’ entrepreneurs had different feelings about the process of negotiating valuation. Valuation was a determinant for forming a relationship, as well as the feelings toward that relationship, with a VC firm.

According to the empirical data, the timing of raising venture capital appeared to be important. A newly-founded company starting talks with VC firms, as in the cases of Chaining and Basing, might be more likely to receive venture capital, but with lower valuation due to unproven technology and market-related factors. The entrepreneurs in this circumstance faced tough negotiations that made them feel unfairly treated. In a situation like Viewing’s, high valuation of the company was difficult for the second and third rounds of financing during the downturn of the
industry. On the other hand, *Placing* and *Sending* already had customers and developed markets, as well as good financial standing. Thus, the entrepreneurs had much stronger negotiation power with VC firms about their valuation. As *Placing*'s entrepreneur described:

“When technology is proven in the market, we increase confidence. When going to next level, we are coming more and more inquiries from different investors, and we involved in investment bank to help us with negotiations, and we create the competitive environment. Then we have the first customer that uses our technology in commercial purpose/environment, and we are able to say to investors no, because we have other options.” (Entrepreneur – *Placing*)

His comment validates that the negotiation power of the entrepreneur increases when the INV is scaling up a business with a proven technology, developed markets, or several established customers. Valuation is dependent upon timing, the specific case’s circumstances, and the external environment. Entrepreneurial negotiation power increases with each round of investment. The more rounds the INV has had, the greater the value of the company. When engaging in different rounds of the financing, the entrepreneurs gradually increase their self-confidence in presenting the business plan and are able to maintain their negotiating strategies. The more discussions the entrepreneurs had with VC firms, the more they understood their negotiating points and could prepare responses to them.

Additionally, the more rounds INVs had with the same VC firm, the more the VC firm was likely to commit to the agreement. As *Viewing*'s entrepreneur described:

“There was no choice of the VC firm to continue investing in *Viewing* because they have invested a lot.” (Entrepreneur – *Viewing*)

If the VC firm lost patience and withdrew to wait for market improvement, the only option was financial loss. Similarly, *Placing* had already received three rounds of financing for the seed and startup phases during the previous five years, and the investors were very committed to the business.
5.6.3 The perceived relational atmosphere

Relational capital should continuously increase until the point of investment decision. Otherwise, the INV may not be able to obtain venture capital. In post-investment activities, while potential conflicts may arise, relational capital may still be increasing, stay steady, or even decrease, as shown in Figure 7. Figure 7 illustrates relational capitalist’s trend in the post-investment stage. The perceived relational capital during pre-investment stage will affect the trend for relational capital in post-investment activities. If the relational trend is increasing, the level of utilization of relational capital will be higher. If it keeps steady, both parties will collaborate and put their effort in nursing the funded INV. If something harming relational capital building between entrepreneur and VCs happens during pre-investment stage, the relational capital in post-investment might be decreasing, in the worst scenario, leading to venture failure.

Fig. 7. Relational capital development trend in venture capital process

*Chaining* is the INV that terminated relational capital formation with the VC firm in the pre-investment stage. The reasons, as analyzed previously, included unfavorable external environment, strong personal characteristics of the entrepreneur relating to control of the company, and unwillingness to compromise. These factors hindered the relational capital building process with the VC firm.

*Sending* received venture capital from multiple VC firms. From the VCs’ point of view, the relational capital increased, but not very dramatically:
“Relationship has up and down with Sending. I think it has increased incrementally. We are confident about their ability to learn, and we already know they can, and we see them with different challenge with so forth. Keeping relationship up requires time investment, not necessary a lot of money. Since both sides get something out of relationship, we don’t feel like burden to develop relationship.” (Venture capitalist – Sending)

The perception of Sending’s entrepreneur is similar. He believes that the coaching received from the VC firm and the mutual cooperation between INV and VC firm are going smoothly.

Placing received three rounds of venture capital: from Finland, the U.S., and Asia. The company’s internationalization was pushed forward by the VC investors, and the entrepreneurial team and VCs divided the responsibilities between them. Notably, Placing was the only case company that received foreign venture capital. The advisor said the international investor team’s support for the INV had increased the valuation of Placing dramatically. She further asserted that because they were more internationally oriented, the likelihood of Placing attracting foreign venture capital was higher.

The U.S. VCs involved in Placing had the background as general partners for Nokia and fully understood the reasoning behind the entrepreneurs’ decisions, based as it was on the Finnish way of doing business. The entrepreneurial team, for their part, also learned from the U.S. VCs about their way of doing business. Mutual understanding attained through cultural experience, learning, and collaboration further increased the willingness to cooperate.

Placing’s entrepreneurs and VCs both perceived the pleasant working relationship, and the VCs were actively exploring foreign markets and pulling other investment into Placing. According to Placing’s advisor, the new investment rounds were actually secured by the current VC firms through their networks. As the entrepreneur, advisor and VCs all seem to surmise, the solid working relationship would help push Placing toward successful venture exit.

Viewing reached exit by acquisition after receiving three rounds of investment. The relational capital with their investors went up and down, especially for the third round of investment while facing industry uncertainty. In general, the VC firms relied on the entrepreneur’s business expertise and prior international network gained from subcontracting for Nokia, thus offering him the flexibility to make decisions. The VCs’ confidence was based on trust between the INV and VC firm generated through the relational capital building process. Because the entrepreneurs
were the decision-makers, few conflicts were actually encountered in the post-investment stage.

The only time relational capital was damaged was when a sharp dilution of shares held by the entrepreneurs occurred, when more money was needed during the dotcom bubble in the early 2000s. Since they have been working together for a long period of time, this increased relational capital during the first two rounds of investment. Viewing’s entrepreneur appreciated the moral support from the VCs, as well as the funding to develop second-generation products during the most difficult times. As the entrepreneur described:

“They were very patient, although they faced high risks. They would have sold the company by lower price, but they waited until the market was open again.”

(Entrepreneur – Viewing)

Although disappointed when devaluation occurred, consistently developed relational capital keeps the relationship stable. The argument could be made that relational capital increases trust and tolerance, especially in uncertain situations. Overall, the relational atmosphere between Viewing and the VC firms moved in a good direction. As a result, Viewing achieved the exit by merger that satisfied both entrepreneur and VCs.

The perceived research atmosphere was dramatically dropping after negotiation meetings between Basing’s entrepreneur and VCs. The disagreement and feelings of unfair treatment that arose in Basing’s case led to ultimate closure of the business.

According to the entrepreneur, it was neither loss, nor gains after several years’ backing by the VC firm. The entrepreneur itself was forced to leave the role as CEO through decisions made by the board directors after VC firm’s involvement. The relationship failure led to the closure of Basing at the end.

In conclusion, the atmosphere created during the process of building relational capital determines the efforts both parties make on behalf of INVs. A longer-term collaboration increases the level of trust between entrepreneur and VCs. Even when something unexpected happens during the partnership, e.g., conflict or the difficulty of industry downturn, if relational capital has accumulated, it can facilitate resolution of the situation.
5.7 Empirical model

This subchapter aims to summarize, by proposing an empirical model illustrated in Figure 8, the data analysis for relational capital formation and utilization between INVs and VC firms. The empirical data strongly emphasizes relational capital formation during the entire investment process and describes relational capital utilization in the post-investment stage as an outcome of the formation process. The empirical data does not point to exact outcomes directly resulting from formation of relational capital. Instead, the data shows that the quality of relational capital formed in the building process can forecast the relational capital development tendencies in the post-investment stage. The relational atmosphere determines the output and willingness to cooperate of entrepreneurs and VCs. In this way, the utilization of relational capital was captured in post-investment activities.

Based on the empirical findings grounded in the interview data, the empirical model of relational capital formation and utilization between INV and VC firm is illustrated in Figure 8. As noted previously, the empirical model focuses on the process of relational capital formation. Relational capital utilization is considered an outcome of relational capital formed between INV and VC firm during the pre-investment stage. The factors identified through empirical analysis are marked in bold and italic font for emphasis in Figure 8.

The empirical data indicates that the motivations are different for formation and utilization of relational capital between INVs and VC firms for internationalization. Most of the case INVs needed venture capital investment for developing foreign markets. However, for the INVs that were in good financial situations, the purpose of raising venture capital was for value-added services, such as management know-how, international networks, and advice on internationalization. VC firms were motivated to invest in INVs mainly based on the assessment of unique technology, entrepreneurial teams, and their own abilities in internationalization. Some of the VC firms simply did not want to lose a prospective investment opportunity by not paying enough attention to the liabilities and risks of internationalization. Since the goals and motivations for internationalization are different between the two groups, several factors are important to formation and utilization of relational capital, based on the empirical results.

The analysis shows that appropriate referrals, such as angel investors and public support organizations, not only connect the INV and VC firm, but also help with the internationalization process, leading to an increase of valuation of the INV.
Appropriate referrals have signaling effects that can increase the trust level between the INV and VC firm and may accelerate the decision-making process of the VC firm.

Interaction between INV and VC firm may create a communication channel through which information can be exchanged. The flow of information can increase the “match” and “fit” between the INV and the VC firm. According to the information gathered through interaction, the entrepreneur and the VCs are able to preliminarily judge whether the INV or the VC firm is the desired company with which to collaborate.

As indicated by the data, the ability of the entrepreneur and team to execute international business operations is one of the most important evaluation criteria for the VC firm. An entrepreneur’s personal and professional experiences and network or other relevant external referral, e.g., an angel investor who can help with the internationalization process by taking a managerial position, can make the INV attractive to a VC firm. Sometimes, a VC firm is opportunistic and does not want to miss any investment opportunity. If the VC firm can find a person through its own network to carry out the internationalization plan, the inexperienced, non-referred INV still can be invested. However, the prerequisites for the INV in this case are an open-minded entrepreneur who is able to accept the candidate recommended by the VC firm, cutting-edge technology showing enough foreign market potential, as well as an industry that fits the VC firm’s investment portfolio.

Valuation of the INV is extremely important for building relational capital, according to the empirical data. If the entrepreneur feels the INV is priced too low, the resulting feeling of dissatisfaction can negatively influence the contribution of the entrepreneur to the INV post-investment. The percentage of shares held by the entrepreneur determines the votes on the board and future control of the INV. Too few shares may decrease the motivation and passion of the entrepreneur for the INV. Therefore, the empirical model adds “psychological ownership” as a factor potentially influencing the willingness to build relational capital with a VC firm and the sweat equity the entrepreneur offers to the INV after investment.

The analysis further reveals that valuation is determined based on the level of entrepreneurial negotiation power with the VC firm. In addition, timing of involving venture capital investment is important for valuation. If the INV is newly-founded and has no track record of backing by other seed-phase investors, the valuation of the INV may be rather low due to unproven technology and market potential. However, if the INV already has an initial foreign customer and has been backed by other investors before starting negotiations with VC firms, the valuation
will be higher than if the INV had none of those things. Accordingly, the entrepreneurs from these INVs may expect higher valuation and more value-added services from the VC firm post-investment. If the INVs are in good financial standing and capable of attracting various VC firms, entrepreneurial negotiation power is much stronger, and the valuation of the INV will be higher.

Human factors, such as an entrepreneur’s characteristics and expectations, have been detected as an important factor that affects the collaboration between INV and VC firm for new venture internationalization. The data shows that almost all of the interviewees commented on the “chemistry” between the entrepreneurs and VCs. If the chemistry between the two is not favorable, a stable level of cooperation cannot be established.

Expectation is a new aspect included in the empirical model. Entrepreneurs’ expectations of VC firms determine with what kind of VC firm the INV will initiate the building of relational capital. Moreover, whether the value-added services meet expectations affects post-investment performance and relational capital’s outcomes.

The external environment brings both opportunities and challenges for the INV raising venture capital. These opportunities and challenges define the thinking and approach that the entrepreneur and VCs take toward one another. Therefore, the external environment is considered a background which is beyond the key factors considered in the empirical model.

The process of forming relational capital creates an atmosphere in which relational capital utilization is achieved. The important outcome of utilization identified through empirical data is to increase the trust level between INV and VC firm, which opens up a communication channel for information exchange. The potential for conflict between INV and VCs is related to their different approaches to scaling up the business. The technology-oriented entrepreneurial team focuses on R&D, while the VCs emphasize launching the products into foreign markets. Relational capital helps them reach mutual understanding and create a strategy alliance whereby either a division of tasks occurs, or joint decisions are made that serve both parties’ needs.

According to the data, the VC firm taking a hands-on approach makes more contribution to finding customers and is more involved in daily international business operations. The VC firm using a hands-off approach mainly aligns strategies through the board and guides the general direction of the INV. The entrepreneurs cite recruiting of personnel for overseas markets and emotional support as the most-needed value-added services offered by the VCs.
Not all of the case INVs were successful in terms of exit. A potential negative alternative is dismissal of the entrepreneur by the board due to unformed or malfunctioning relational capital. Both the entrepreneur and the VCs claim that it is a learning process. Especially after the entrepreneur learns from relational failure, mistakes, and experiences, he or she can modify the relational approach to working with VC firms and bring that learning to the next venture.

Fig. 8. Empirical model of relational capital formation and utilization between INV and VC firm
To summarize, the empirical model argues that the core of relational capital between INV and VC firm is the process of forming relational capital. Relational capital purposely formed creates a relational atmosphere in which entrepreneurs and VCs contribute to the INV during post-investment activities. The lessons and experience learned through relational interaction post-investment change the ideas and approaches that entrepreneurs use to work with VCs. As a result, relational learning outcomes will be further applied to form relational capital with other VC firms.
“Learning without thinking means wasted work; thinking without learning is dangerous.”

– Confucius
6 Discussion

This chapter provides an evidence-based discussion of the findings and results related to the influential factors affecting relational capital formation and utilization and its importance to venture capital-backed INVs. The chapter continues with answering the two main research questions defined earlier, and provides relational capital as a view into the relationship between INVs and VC firms for new venture internationalization. Finally, the chapter ends with a discussion of the conceptual model of the study.

6.1 Overview and discussion of findings

This study takes relational capital as a means through which to view the INV and VC firm dyad relationship. It further explores the factors affecting the formation of relational capital and the outcomes of relational capital for new venture internationalization. The empirical findings support the definition of relational capital detailed in the literature review as being the level of trust and transparency developed in a course of interactions between INVs and VC firms that leads to positive venture capital decisions and value creation through interaction in post-investment activities. This definition is consistent with Clercq and Sapienza’s (2006) article in which trust, goal congruence, and social interaction are defined as the dimensions of relational capital in the venture capital investment context.

The results suggest that the formation of relational capital should be carefully considered by both parties of the dyad in the pre-investment stage so as to satisfy both entrepreneur and venture capitalist. In fact, relational capital is utilized within a relational atmosphere that is created as a result of the relational capital formation process. Any unpleasant surprises or dissatisfaction occurring in the pre-investment stage will continue in the post-investment stage of utilization of relational capital and will affect both parties’ motivations for open discussion, information exchange, and the amount of tacit knowledge they contribute to the INV. In effect, the quality of the relational capital as perceived by the INV and VC firm can lead to either successful or unsuccessful venture exit.

When new venture internationalization is a primary reason for raising venture capital, controlling liabilities and risks becomes an important consideration for the VC firm upon initiating the relationship. Introduction by appropriate referrals of the entrepreneur to the VC firm is the ideal way of approaching a VC firm. Backing by angel investors and participation in incubating activities organized by third-
party business support organizations increases the credibility and trustworthiness of the INV’s ability to operate in an uncertain international environment. Additionally, external investors or support organizations that have shaped the international business plan and strategies of the INV may increase the valuation of the INV and the negotiation power of the entrepreneur with the VC firm. Interactions between INV and VC firm facilitate information exchange and knowledge transfer, which results in mutual understanding and may help solve the problem of goal incongruence post-investment.

In addition to the prior discussion on relational capital regarding the importance of trust, interaction, and goal congruence (Clerq & Zapienza 2006), the findings add other factors to increasing the understanding of the relational capital formation and utilization process for new venture internationalization. The first factor, control rights over the INV by the entrepreneur, promotes psychological ownership on the part of the entrepreneur. From the entrepreneur’s perspective, possession or non-possession of control rights over the INV affects his or her psychological ownership (Townsend et al. 2010), i.e., whether he or she is seen as the INV founder or just another employee. These kinds of emotional feelings can greatly affect the motivation of the entrepreneur (Wasserman 2016) to form relational capital or, more to the point, to sign the investment agreement.

Once the investment agreement is signed, these feelings will carry forward to the post-investment stage and determine the willingness of the entrepreneur to have open discussions and contribute sweat equity to the INV. As Cable and Shane (1997) argued, the ability of both parties to maximize gains cannot survive without an entrepreneur’s strong commitment, emotional involvement, and identification with the company.

From the venture capitalist’s agency-based perspective, gaining control rights over the INV can be a mechanism that prevents entrepreneurs from opportunistic behavior and saves the agency cost of the VC firm. Therefore, gaining control rights compels INVs and VCs to establish more formal relationships or agreements than would be expected of an informal social relationship. The control rights over the INV after venture capital investment greatly affect the willingness of the entrepreneur and VCs to collaborate.

Relational capital is accumulated through interaction between entrepreneurs and VCs. Therefore, the characteristics of entrepreneurs, as a human factor, are important for building relational capital, especially in terms of negotiating control rights for INVs and the entrepreneurs’ degree of insecurity about the future of the
venture. Their expectations for value-added services from VC firms might drive the
direction of their relational tendencies in the post-investment collaboration.

The findings also implicate that the external environment surrounding the
entrepreneurs and VCs has an impact on their decisions and shapes their thinking
toward the venture capital industry as a whole. This can also be interpreted as luck
or opportunity, as when the environment offered luck and opportunity for Placing
and Viewing, or as when it brings difficulty or challenge to forming a relationship
between the INV and VC firm, as experienced by Chaining.

Based on the empirical data, it is not possible to exactly differentiate the value-
added services that are appropriated through relational capital from those that are
not. However, the findings suggest that the formation of relational capital creates a
relational atmosphere determining output from entrepreneur and VCs. The
empirical findings show that an increased level of trust between INV and VC firm
as a relational outcome minimizes the amount of time spent on monitoring and
offers flexibility to both entrepreneur and VCs to make decisions on
internationalization, as shown in Sending’s and Placing’s cases.

Relational capital increases mutual understanding about embedded strengths
and knowledge during the relational capital formation process, which enables the
parties to find a suitable working approach, e.g., division of tasks between
entrepreneurial team and VCs, as in Placing, and a hands-on or hands-off approach
on the part of the VC firm based on the entrepreneur’s experience and network
resources. The research results answer the question posed in the study by Busenitz
et al. (2004), which pointed out that venture capital involvement, e.g., a hands-on
or hands-off approach, has not produced consistent results in terms of venture
performance.

This study argues that INV performance cannot be correlated with different
levels of venture capital involvement, i.e., that a hands-on approach improves
venture performance while a hands-off approach causes poor performance, or vice
versa. In fact, relational capital compels entrepreneurs and VCs to find an
appropriate approach that suits both parties’ needs, regardless of whether the level
of involvement is high or low. Accordingly, a mutually agreed upon level of venture
capital involvement will improve INV performance, because this approach meets
both entrepreneurs’ and VCs’ expectations.

The results also suggest that a foreign VC firm brings more value-added
services to internationalization strategy, foreign market exploration, and
development, as shown in Placing’s case. Further, because of their small size and
lack of foreign investment experience, Finnish domestic VC firms are better
equipped to offer support for recruiting staff or moral support for the internationalization process of the new venture. These findings are consistent with anecdotal evidence found by Sapienza et al. (1996), which argued that when VCs had great investing and operational experience in a relevant industry and foreign market, the VC firm adds the most value to the INV, especially when the entrepreneur is inexperienced.

6.2 Discussion related to the research questions

The objective of the study was to understand the importance of formation and utilization of relational capital in the dyadic relationship between new venture internationalization and venture capital. The study has answered two main research questions. The first research question is concerned with the role relational capital plays in raising venture capital for new venture internationalization:

1) How do INVs develop and utilize relational capital as a means of obtaining venture capital investment for new venture internationalization?

This study aimed to answer the first research question by understanding the role of relational capital in raising venture capital and identifying the factors that influence relational capital formation in the INV/venture capital context. To start with relational capital formation, the prerequisite for study was to understand and explore the motivation, perceived liabilities, and risks for new venture internationalization experienced by entrepreneurs and VCs. The results showed that entrepreneurs who decided on early internationalization did so because of the nature of their products and limited domestic markets. They paid little attention to foreign market potential and costs associated with new venture internationalization. However, the VCs were concerned about the risks and costs associated with internationalization, costs that early-stage ventures operated by small entrepreneurial teams were not able to afford. Therefore, controlling for liabilities and risks naturally became a major factor contemplated by VC firms when deciding whether to form a relationship with an INV. The study identified controlling for liabilities and risks of the INV as an important factor influencing a VC firm’s decision.

Due to the smallness of the INVs, the assets often center around the entrepreneur: their experience, knowledge, and network relationships (Ruzzier et al. 2007). This study found that the entrepreneur/or entrepreneurial team and their
relational capital for executing internationalization operations became an important criterion for VCs to determine whether INV was able to control for liabilities and risks. This finding was consistent with prior literature on new venture evaluation of a specific investment proposal that is primarily determined by the entrepreneur’s or entrepreneurial team’s capability (Chen et al. 2009, Franke et al. 2008, Kaplan & Stömberg 2004, MacMillan et al. 1985, Robinson 1987, Shepherd 2000), including experience (Patzelt 2010, Petty & Gruber 2009), leadership (Clarysse et al. 2005, Muzyka et al. 1996), competence and capabilities (Fried & Hisrich 1994, Muzyka et al. 1996), complementarity (Clarysse et al. 2005, Franke et al. 2008), and characteristics (Chen et al. 2009, Sandberg & Hoffer 1987) at the pre-investment stage.

As empirical evidence indicated, VCs paid attention to the relational capital of the entrepreneur and the track record that the INV had at inception, e.g., incubating process, initial startup funding and grants, angel investment or participation in a public organization’s project for new venture internationalization, because they realized that entrepreneurial teams with limited internationalization knowledge and experience actually rely more on external sources, including VC firms or network partners. Carpenter et al. (2003), Carpenter & Petersen (2002), and Fernhaber & McDougall-Covin (2009) supported the finding that unless the VCs were in a position to place an internationally experienced director onto the venture board and similarly experienced managers into management positions, VCs might see internationalization as too risky (Carpenter et al. 2003, Carpenter & Petersen 2002), and thus prefer to pursue a domestic strategy.

The empirical results showed that those INVs founded by inexperienced entrepreneurs and that had been backed by an angel investor and received initial startup funding from a public organization supporting high-tech new venture internationalization had a greater chance of being funded by INVs. The empirical results acknowledged not only that appropriate referral was able to connect INV and VC firms, but also that referral increases the credibility and valuation of the INV. Therefore, appropriate referral serves as a factor affecting the establishment of a relationship with VC firms and is important for building relational capital with stakeholders around the business community. Conversely, the results show that if the VCs acknowledged the motivation, skills, and capabilities of the entrepreneur or the entrepreneurial team, they might feel confident enough to take the risk of allocating a higher level of investment, even if the VCs’ confidence in their own internationalization capabilities is not very high, as evidenced in the case of Viewing. This result is consistent with Payne et al.’s (2009) study that VCs make
investment decisions by looking at both the entrepreneur’s and the VC’s own capability for early internationalization.

Valuation of an INV was a central matter for both the entrepreneur and VCs in the deal-structuring stage of the venture capital decision-making process (Cumming & Dai 2011, Engel & Keilbach 2007, Festel et al. 2013, Gompers et al. 2010, Hsu 2005). This study did not directly deal with calculating the valuation of the INVs; instead, this study approached the valuation of the INV from two perspectives: the control rights of the INV and the amount of shares sold to VC firms. These two emerged from the data.

Control rights of the funded INV was surprisingly important from the entrepreneur’s perspective in deciding whether to form a relationship with a VC firm, according to the empirical model. The major concern indicated by the empirical evidence from the entrepreneur’s viewpoint was the loss of control over the INV after acquiring venture capital, and their worry about the uncertainty of the future of the founded INV. Fear of losing control of the firm after VC investment was supported by Shepherd and Zacharakis’s (2001) as well as Ojala and Heikkilä’s (2011) study.

The empirical results indicated that the valuation and the amount of equity shared with the VC firm had a great influence on the entrepreneurs’ psychological ownership. A valuation of the INV that was too low, or if the percentage of shares held by the VC firm was too high, decreased the motivation of the entrepreneur and could lead to affective conflict capable of producing suspicion, distrust, and hostility (e.g., Amason & Sapienza 1997, Ensley et al. 2002, Higashide & Birley 2002) between entrepreneur and VC firm in the post-investment stage. The results suggested that beyond mathematical calculation, non-financial performance (e.g., goodwill) should be taken into account and managed, such as an evaluation of the innovation capability and inter-firm network of the INV (Zheng et al. 2010), as well as relational capital developed with the entrepreneur. The finding indicated that the valuation of the INV determined the psychological feeling of entrepreneurs, e.g., whether being fairly treated or whether being a founder or only the employee. As a consequence, VC firms should handle the valuation of the INV carefully.

This study also added another two emerging factors that affect the formation of the relationship between INVs and VC firms: human factors and luck or opportunity. The human factor related to the personalities of the entrepreneurs, determining the degree of willingness for cooperation with VC firms in building the relational capital process, as well as the abilities of the entrepreneurs to negotiate with VC firms, e.g., experienced or inexperienced young entrepreneur.
Luck or opportunity related to uncertainty, either facilitating or hindering relational capital formation with VC firms because of the external environment.

The second main research question is related to value appropriation from relational capital through post-investment interactions between INV and VC firm in the venture capital process:

2) How is relational capital between INVs and VC firms utilized for new venture internationalization after the venture capital investment agreement has been signed?

The second question is approached from the angle of the relational atmosphere created through the relational capital building process in the pre-investment stage. The research results showed that a relational atmosphere in which the INV and VC firm work together in the post-investment stage is created through the relational capital formation process in the pre-investment stage. Instead of figuring out the concrete outcomes directly from relational capital and measuring scale, scope, and speed of internationalization after venture capital involvement as in earlier studies (George 2005, LiPuma 2006, Lockett et al. 2008, Lutz & George 2012, Smolarski & Kut 2011, Zahra 2007), this study argues that outcomes of venture capital involvement for new venture internationalization are achieved through the perceived relational atmosphere in which value is appropriated and maximized.

A pleasant relational atmosphere can bring about the following benefits: first, the relational atmosphere determines the amount of effort the entrepreneur and VC$s$ are willing to contribute for INV internationalization, as well as value appropriated from the VC firm’s network for potential customers, investors, and other resources. The entrepreneur’s effort has been found to be important for a VC-backed venture’s success (Wasserman 2003). Second, developing effective relational capital can increase the level of trust and mutual understanding between entrepreneur and VC$s$ to achieve goal alignment by maintaining focus on the real business. This is similar to the study by Sapienza (2010), which argues that a proactive approach should be adopted to form a business relationship between the startup and VC firm to understand the specific issues of mutual interest early in the relationship.

Third, a congenial relational atmosphere can create an environment that encourages open discussion to facilitate information exchange. This is important, because the entrepreneur and VC$s$ hold different information advantages toward INV internationalization. The findings are supported by the research by Shepherd and Zacharakis (2001), which indicates that open discussion serves as a catalyst for
building trust in the entrepreneur/venture capitalist relationship. Fourth, relational capital increases the chance of finding an appropriate working approach that fits both parties through open discussion, information exchange, and understanding of the strengths of each party.

The mutually agreeable working approach offers operational flexibility for both entrepreneur and VCs to conduct international business operations. The results support the Smolarski and Kut study (2011), demonstrating that too much monitoring and restriction by the VC firm has negative effects on the internationalization performance of the INV, because the entrepreneur’s demands for operational flexibility to deal with uncertainties encountered in new venture internationalization are not met. Finally, it should not be forgotten that an unpleasant relational atmosphere may also create relational challenges leading to failure of the VC-backed INV.

Unlike prior studies focusing on internationalization performance of VC-backed INVs (George 2005, LiPuma 2006, Lockett et al. 2008, Lutz & George 2012, Smolarski & Kut 2011, Zahra 2007), this study proposes a new element called “relational atmosphere” that is created during relational capital formation in the venture capital decision-making process. This study implicitly implies that internationalization performance can improve in a congenial relational atmosphere due to the increased trust level, maximized efforts, and information exchanged between entrepreneur and VC firms, as occurred in the cases of Placing and Viewing. On the other hand, a perceived unpleasant relational atmosphere can lead to unsuccessful exit, as shown in the case of Basing.

6.3 Conceptual model: a posteriori model

On the basis of the discussion above, as well as the theoretical model (Figure 5) and empirical model (Figure 8), this study constructs a conceptual model, shown in Figure 9. The conceptual model illustrates the financing of entrepreneurial INVs by turning relational capital into venture capital.

The conceptual model proposes that financing for entrepreneurial INVs occurs by turning relational capital into venture capital investment. According to the coding system, initially, the categorizations were organized on the basis of the theoretical model and empirical data. New categories were identified, analyzed, and added to empirical model as shown in Figure 8. When coming to the presentation of the research results, illustrated in Figure 9 (conceptual model), the
categories were further refined and organized on the basis of INV-related factors, behavioral factors, and VC firm–related factors in the pre-investment stage.

The INV-related factors mainly related to entrepreneurs’ opinions and their interpretation of relational capital in the venture capital raising process. INV-related factors create the context of new venture internationalization for viewing venture capital studies, because an increasing number of entrepreneurial INVs are looking for venture capital investment. Relational capital can emerge only when the INV’s technology, team, and other elements meet the criteria of the VC firm. VC firm–related factors are important for the formation of relational capital, but the VC firms should conduct due diligence in any case in order to secure the quality of the INVs. VC firm–related factors summarize the important factors in how VC firms evaluate INVs, based on the VC literature and empirical analysis of the VC interviews. Behavior-related factors emerging from the data have been found to be extremely important in the relational capital formation process, because the relational aspect is related to human behavior and actions. In the context of INV, how entrepreneurs and VCs perceive the risk and uncertainty of internationalization, as well as how relational capital influences their mindsets, plays an important role in the process of building relational capital. The entrepreneur’s and VCs’ perceptions of activities undertaken during the course of interactions in the relational capital building process shape their attitudes toward the relationship. The relational capital formation process may go through a series of ups and downs, may collapse altogether, or may be revised and rebuilt in any phase of the investment process. The entrepreneur may withdraw his proposal for venture capital investment, as may the VC firm, if either party is reluctant to collaborate.

Compared with the theoretical model, the conceptual model has added the relational capital atmosphere as an outcome of the relational capital formation process. In the coding system, the relational atmosphere has emerged as a major theme on the basis of the perception of entrepreneurs concerning the degree of satisfaction perceived in the relational capital formation process with VC firms. The research results show that the relational capital formation process creates a relational atmosphere through which relational capital utilization is achieved for INV internationalization. The relational atmosphere particularly determines the amount of effort and information that entrepreneurs are willing to contribute to the funded ventures after the venture capital investment decision has been made. The relational atmosphere serves as a bridge between relational capital formation and utilization in the INV/VC firm relationship.
Fig. 9. The conceptual model of financing entrepreneurial INVs by turning relational capital into venture capital
According to the empirical model, various kinds of value-added services and supports for the INVs have been obtained from VC firms for new venture internationalization. The empirical model has presented the findings in detail on the basis of the empirical data. When discussing the study’s results in the conceptual model, the detailed value-added services that the INVs obtained from the VC firms can be further refined to three categories, according to the coding system. The three categories are the provision of tangible resources, intangible resources from the entrepreneur and the VCs, and relational failure. The division of the resources into tangible and intangible resources is based on the literature of the resource-based view. Conversely, a non-performing relational atmosphere may lead to relationship failure, including not obtaining venture capital investment or an unsuccessful exit after venture capital investment. As a separate category, relational failure has emerged from the data in the context of the study of INV and VC firms. Relational failure does not necessarily mean that the INVs have not received any tangible or intangible resources from VC firms or vice versa; instead, it means that relational capital utilization has not been on the right track due to, for example, relational frustration or a lack of trust, leading to a failure to raise venture capital or unsuccessful exit after venture capital allocation.
“By three methods we may learn wisdom: First, by reflection, which is noblest; second, by imitation, which is easiest; and third by experience, which is the bitterest.”

— Confucius
7 Conclusions

This chapter concludes the study and discusses the contribution of the thesis. The conclusions of the study fall into three levels of discussion: a discussion of relational capital and INV literature in the context of the INV and VC firm; a discussion of relational capital and VC literature, as well as the contribution this study has made to VC literature; and a discussion of relational capital as a means of understanding the INV/VC firm relationship. This chapter also presents the theoretical contribution and practical implications of the study before discussing the merits and limitations of the study, leading to an agenda for further research. Chapter 7 ends with the research summary for this study.

7.1 Conclusions of the study

The fields of research this study has touched on are international entrepreneurship, social capital, and venture capital. More precisely, the focus has been on the literature relating to INVs’ network relationship, the venture capital investment process, and relational capital.

Relational capital and INVs in the context of VC financing

In the INV literature, the network relationship has been regarded as a facilitator for INVs to gain access to and attain resources that cannot be owned by INVs (McDougall 1994). However, what INV managers actually do to find, develop, and use these relationships has not yet been extensively studied (Chetty & Holm 2002, Loane & Bell 2006, Sullivan Mort & Weerawardena 2006). This study has investigated an INV/VC firm relationship and explored what entrepreneurs have done and how in order to form and use relationships with VC firms. Relationship formation and utilization between INVs and VC firms to internationalize INVs has been studied by exploring influence factors and outcomes resulting from the INV/VC relationship.

The network is important for INVs suffering concurrently from liabilities of foreignness and newness, as a key benefit of a network relationship for the entrepreneurial process is the access to information, advice, and emotional support, as well as its signal and reputational effect. The foreign market–related information, advice, and connections obtained through a network relationship help in new venture internationalization (Coviello & Munro 1997, Ellis 2011). The findings of
this study suggest that VC firms, particularly experienced and foreign VC firms, involved in INV add great value to the internationalization of new ventures. However, domestic VC firms without foreign investment experience cannot achieve similar results. This argument is consistent with Sapienza et al.’s (1996) findings that the greater investing and operational experience of the VC firm in a relevant industry, the more value that VC firm can add to the venture. The study results have further clarified that the value that VC firms add to INVs’ internationalization process includes recruiting key staff for internationalization, acquiring the initial foreign customer and specific market exploration, formulating foreign market entry strategies, providing emotional support, and bringing additional financial capital investment.

The signal and reputation effects of network relationships help new ventures to offset the lack of a track record and the limited legitimacy resulting from newness (Shane & Cable 2002). The results of this study have shown that the VC firm makes it possible to pull in another VC firm as a syndication partner to invest in a funded INV. Although an INV still needs to go through the formal investment process, the procedure and time of the VC decision-making process is simplified and shortened. In addition, the study also indicates that the active networking of entrepreneurs in both domestic and foreign market allows INVs to find appropriate referrals. Through these appropriate referrals, INVs increase their chance of being exposed to the suitable VC firms by the referrals’ reputation, thereby increasing the likelihood of initializing relational capital formation with a VC firm. The result of this study has indicated that the network of an INV is able to generate VC ties at the inception stage of the venture and leverage resources around VC firms for new venture internationalization. This result differs from Coviello and Cox’s (2006) study, which reported that an INV’s network seemed to be more important for generating organizational and human capital than it was for financial capital.

Relational capital and the VC literature

With regard to the VC literature, a stream of prior venture capital research focuses on the VC’s perspective during the venture capital process. The researchers have conducted work in developing rigorous VC investment criteria, understanding how VC firms monitor their portfolio companies, exploring the kinds of value-added services and in which conditions VC firms provide value-added services to their portfolio companies, as well as the entrepreneur/VC relationship. However, most of the studies have been conducted on the basis of a large sample survey from VC
firms or VCs’ interviews. The VCs’ perspective dominates the field of VC research. In contrast to the previous research, this study is entrepreneurial-centric and emphasizes the entrepreneur’s influence on venture capital investment decisions. The study results have shown that entrepreneurs can improve the likelihood of being exposed to VC firms by active networking. The networking process of the entrepreneur makes it possible for INVs to connect to the appropriate referrals, such as angel investors, public organizations, and incubators that support the international activities of startups. In Finland in particular, startup capital from public organizations and foundations supporting high-growth, internationally focused technological entrepreneurial startups is an initial source of funding. Records of being funded by public foundations and organizations can increase the credibility of INVs for VC firms and approval for the functioning of technology. This study results have shown that INVs backed by angel investors or that received grants to start up international business are mostly the ones that are invested in by VC firms.

In relation to VC selection criteria, this study adds new elements to the VC decision-making process. From an entrepreneur’s perspective, this study has indicated that entrepreneurs can increase their negotiating power with VCs in the valuation of INVs through initial foreign customers, the current financial situation, the industrial situation, and initial rounds of VC investment. This study measures valuation in terms of control rights for INVs and the number of shares sold to entrepreneurs, their consequences, and the impact on psychological feelings. On the basis of the results, a valuation that satisfies both parties makes the entrepreneur feel fairly treated by VCs and so increases the likelihood of the entrepreneur perceiving a positive relational atmosphere. The classic VC investment decision-making process involves rigorous evaluation based on concrete facts, such as team capabilities, the technology, and the market, but this study suggests that besides the mathematical methods of calculation for the valuation of an INV, such as discounted cash flow (Sahlman 1990, Scarlata & Alemany 2010), it is critical to manage relational factors beyond financial calculations during negotiations between the entrepreneur and VCs. VCs should take behavioral factors into account when preparing an investment term sheet and should think carefully about the entrepreneur’s psychological ownership of the firm and their willingness to control funded ventures.

The VC literature has focused on monitoring and value-added services in the post-investment stage of the VC process. This study adopts relational capital as a lens and argues that it is only through a positive relational atmosphere, perceived
in the relational capital formation process of the pre-investment stage condition that entrepreneurs are willing to offer sweat equity as such in the post-investment stage, leading to the positive performance of the INV during the new venture internationalization process. The positive relational atmosphere leads to an increasing level of trust and open discussion that facilitates the exchange of information, thereby allowing INVs and VC firms to find an appropriate working approach in the post-investment stage. The findings are supported by the research of Shepherd & Zacharakis (2001), which indicates that open discussion serves as a catalyst for building trust in the entrepreneur/venture capitalist relationship. This study implies that mutual developed relational capital can offset opportunistic behavior between both parties thanks to the increased level of trust built during the relational capital building process. By contrast, an unpleasant relational atmosphere can also be generated during relational capital formation process, leading to unsolvable problems, such as affective conflicts, a decrease in the willingness to cooperate or reducing the sweat equity the entrepreneur contributes to the funded ventures, and agency problems. As a consequence, VC firms may take action, through a board meeting, to replace the founder as CEO. The lack of an entrepreneur’s passion and contribution, in worst-case scenarios, results in VC-backed INV failure.

The study indicates that relational capital formation and utilization have initially helped entrepreneurs raise venture capital and that the relational atmosphere perceived during the pre-investment phase will determine the future of a funded INV in terms of the amount of contribution offered by the entrepreneur as well as the efforts from VC firms. Thus, this study considers that the venture capital process for INVs is a process of forming and utilizing relational capital between INVs and VC firms.

**Relational capital as a view to INV/VC firm relationship**

This study also takes a relational capital as a view to INV/VC firm’s relationship. In the venture capital context, the agency problem (Jensen & Meckling 1976, Kaplan & Strömberg 2003a) resulting from separate ownership and control in companies has always been a problem for VCs. This study has taken relational capital as a holistic view to increase understanding of how agency problems could be initially avoided by carefully formed relational capital and resolved by utilization of the relational capital built between the INV and VC firm.
The principal/agent approach to investigating the entrepreneur/venture capitalist relationship comes from the agency perspective and results from separate ownership and control (Jensen & Meckling 1976, Kaplan & Strömberg 2003). Agency problems are mainly identified as goal incongruence, information asymmetry, and moral hazards (De Clercq & Zapienza 2001, Eisenhardt 1989a). In order to resolve the agency problems, VCs tended to reduce opportunistic entrepreneurial behavior and control entrepreneurial performance by conducting detailed due diligence, writing comprehensive contracts, and monitoring (Sapienza & Gupta 1994, Manigart et al. 2002).

This study criticizes these formal controlling methods used by VCs. While they may partially resolve the agency problems, too much control exerted by VC firms decreases the motivation and effort of the entrepreneur after venture capital investment, based on the empirical results. Moreover, the agency perspective also neglects the entrepreneurs’ power in the relationship (Lehtonen 2006) and overlooks entrepreneurs’ willingness to collaborate. Finally, VCs are just as prone to acting opportunistically upon the interests of the entrepreneur (Shane & Cable 1997).

This study is aligned with the thinking of the procedural justice theory, which considers the relational aspect of the entrepreneur/venture capitalist relationship. The study result is consistent with Huse’s (1993, 1994) findings, drawing on relational contracting theory, that clarify the critical role that trust and positive interpersonal relations play in board effectiveness and explain how trust and interpersonal relations were developed by procedural justice theory.

Nonetheless, this study differs from procedural justice theory, which is based on the assumption that the entrepreneur is dependent on the VC firm’s capital and expertise to develop the business (Lehtonen 2006). A similar assumption is adopted by the stewardship theory and applied to examine the entrepreneur/venture capitalist relationship. By taking the relational capital view, this study acknowledges that the power of the entrepreneur is equal to that of the VC firm and hears the entrepreneur’s voice in interpreting the relationship with VCs.

The empirical results demonstrate that the key factors influencing the formation of relational capital should be well-managed before signing the investment contract. Well-developed relational capital increases mutual understanding of each other’s needs, which helps keep their goals aligned and appropriates more value from both parties for new venture internationalization. That relational capital helps to maintain goal congruence post-investment is in accordance with Clerq and Zapienza’s (2006) study. Understanding the relational
capital that entrepreneur and venture capitalist bring to the relationship may change the overall costs of funding, e.g., saving monitoring costs and staying focused on the real business. Mutually developed relational capital also acts as a control mechanism, preventing opportunistic entrepreneurial behavior.

Entrepreneurs might also take the opportunity to obtain more valuable links from the VCs’ network for the next round of financing and internationalization activity (Newbert et al. 2013). Also as an outcome of relational capital, new ventures can increase international exposure that enhances their survival and growth in foreign markets (Fernhaber & Li 2013). The increased valuation of the INV when moving toward successful exit helps the investors to recycle their capital and attract new funds, thus increasing the reputation of the VCs in the local equity market to attract, reallocate and reward investors’ capital (Guler & Guillén 2009).

Therefore, relational capital creates a win-win situation for both INV and VC firms. It is also arguable, based on the research results, that if relational capital encounters problems in the formation process, these problems would most likely continue into the utilization stage and potentially even lead to venture failure. While VCs are still able to use the board as a monitoring instrument to intervene in the decisions of the entrepreneur, e.g., dismissal of the INV founder, they subject themselves to the risks of unsuccessful venture exit as well as losses for both entrepreneur and VCs.

As a general conclusion for this study, maintaining a congenial relational atmosphere brings mutual benefits for both INVs and VC firms contemplating new venture internationalization. The relational capital view can be considered another instrument in the INV/VC firm relationship, under the assumption that both entrepreneur and VCs work cooperatively toward the goal of successful new venture internationalization.

### 7.2 Theoretical contribution

On the basis of the conceptual model elaborated and the conclusions of the study discussed above, several propositions have been developed to present the theoretical contribution of the thesis. This study is designed to study relational capital formation and utilization between INV and VC firms for new venture internationalization, and aims to capture how INVs have developed early international processes alongside building up and utilizing relational capital with their financial resource-provider VC firms. The study results have shown that INVs have increased the likelihood of being funded by VC firms by actively building
relational capital with VC firms and stakeholders. The relational capital utilization, including the sweat equity contributed by the entrepreneurs and value-added services offered by the VCs, is determined by the relational capital accumulated during the relational capital formation process between the INV and VC firm. From observing the role of relational capital between INV and VC firm in the venture capital investment process, the first proposition is as follows:

**Proposition 1.** The process of venture capital investment is influenced by the process of relational capital formation between INV and VC firms.

In order to better understand the relational capital formation process between INV and VC firms, this study has investigated the factors that might influence relational capital formation, arriving at the second proposition of the thesis:

**Proposition 2.** Relational capital formation between INV and VC firms is influenced by INV-related factors, VC-related factors, and behavior-related factors.

In addition, this study suggests that besides other influencing factors, INV and VC firm–related factors, behavior-related factors (including trust accumulation), VC risk-taking behavior, particularly, control rights for INVs, entrepreneurs’ power, and psychological ownership are extremely important for entrepreneurs in making up their mind to sign the VC investment agreement. The behavior-related factors become the major contributors that determine the amount of sweat equity offered by entrepreneurs and the amount of information exchanged between INV and VC firms in post-investment collaboration.

The relational atmosphere has emerged in this thesis as a bridging belt between relational capital formation and utilization. Relational capital utilization for INVs in post-investment activities is achieved under the relational atmosphere created in the relational capital formation process. Relational capital formation creates two very different relational capital atmospheres. The congenial relational atmosphere facilitates information exchange, promotes open discussion, and increases the level of trust, leading to the finding of an appropriate working approach between INV and VC firms. As a result, it enhances the utilization of relational capital between INV and VC firms and may guarantee a positive exit. The unpleasant relational atmosphere may produce affective conflicts, distrust between INV and VC firms.
leading to negative performance results or even bankruptcy. The third proposition is presented below:

**Proposition 3.** The relational capital formation process between INV and VC firms in the pre-investment stage creates a relational atmosphere, determining the degree of relational capital to be utilized between INV and VC firms in post-investment activities.

This study offers relational capital as an alternative approach to investigating the INV/VC firm relationship. The study results indicate that it is worth building a congenial relational atmosphere and promoting collaborative behavior between INV and VC firms. Both will benefit from the relational capital built during the VC investment process. For entrepreneurs, actively building relational capital with the VC may increase the chance of getting VC investment, as well as obtaining tangible and intangible resources from the VC firm for new venture internationalization. For VC firms, the relational capital with INVs and third parties helps VC firms obtain an increased amount of valuable and voluntary information about the INVs, thus increasing the chance of making a good investment decision. Creating a congenial relational atmosphere also motivates entrepreneurs to offer greater sweat equity in post-investment collaboration. The fluent flow of information between INV and VC firms saves the cost of monitoring. The collaboration between INV and VC firms helps to achieve goal alignment, resolve conflicts by accumulated trust, and reach agreements on an appropriate working approach, leading, as a consequence, to a positive exit. Therefore, the fourth proposition is developed as follows:

**Proposition 4.** Relational capital promotes collaborative behavior between entrepreneurs and VCs and brings mutual benefits to both INV and VC firms.

This study contributes to INV literature by providing understanding of how an INV is developed and backed by a VC firm through the formation and utilization of relational capital. It further offers instruction to entrepreneurial INVs for how to leverage venture capital as both a financial and networking resource in the early internationalization process. In the discussion of INVs, much effort was devoted to studying the importance of the entrepreneurial firm’s relationships, yet little is known about how entrepreneurs find, develop, and use different types of relationships for internationalization (Sigfusson & Harris 2013). This study fills the gap by investigating the dyadic INV/VC firm relationship and clarifying how
entrepreneurs have managed to form and utilize relational capital with VC firms for new venture internationalization.

There is a stream of venture capital literature indicating that the VC firm increases the scale, scope, and speed of new venture internationalization (George 2005, LiPuma 2006, Lockett et al. 2008, Lutz & George 2012, Smolarski & Kut 2011, Zahra 2007). However, few studies have investigated how the scale, scope, and speed of new venture internationalization are enhanced by the VC firm. This study has taken relational capital as a focal point, exploring the role it plays in the INV’s raising of venture capital, as well as the role it plays in the internationalization process of the INV after venture capital involvement. Using relational capital as a lens through which to view the INV’s and VC firm’s relationship helps shed new light on the venture capital literature by focusing on the interactions between the INV and VC firm.

This study extends the venture capital literature by providing relational capital as a holistic view to the INV/VC firm relationship and considers the venture capital process as a relational capital building and utilizing process between the INV and VC firm. The study has taken both the entrepreneur’s and VCs’ perspectives into consideration and promotes the collaborative behavior of the entrepreneur and VCs. The relational capital view is different from the agency perspective in that it assumes the entrepreneur is an opportunistic agent who might not act upon the interests of the VC firm as principal. The relational capital view focuses on the relational aspect of the relationship as well as the power and voice of the entrepreneur. As a result, it does not consider the entrepreneurial INV as a subordinate of the VC firm, as assumed by the procedural justice theory and stewardship theory (Koskinen et al. 2014, Lehtonen 2006).

This study also contributes to social capital theory by studying relational capital as a dimension of social capital in terms of the role it plays in the INV/VC firm relationship. Relational capital has been found to be important for raising venture capital (Liao & Welsch 2005), and offering more advice to entrepreneurial new ventures in post-investment stage (Lim & Cu 2012). However, how relational capital works had not yet been studied until this research was conducted. This study has contributed to answering this research problem by identification of the factors related to the INV, the VC firm, and human behavior as being important for forming relational capital between entrepreneurial INVs and VC firms. It also indicates that the relational atmosphere created during the relational capital formation process is related to the performance of INV internationalization after venture capital investment.
Financing is a key issue in the creation of an entrepreneurial firm (Gartner 1985), and venture capital is considered an important source of funding for high-risk technology ventures. As prior research indicated (e.g., Croce et al. 2013, Pratch 2005, Sapienza et al. 1996), venture capital provides not only financial resources, but also management know-how that is important for an INV’s survival and growth. This study offers new insights into how an INV is able to raise and utilize venture capital for the early internationalization process, including resolving resource constraint problems, overcoming liabilities of internationalization, and leveraging needed resources through the formation, development, and utilization of relational capital with a VC firm.

7.3 Practical implications

This study offers practical implications for three target groups. First, it has implications for entrepreneurs who aim to raise venture capital for new venture internationalization and are successful in their post-investment collaborative activities. The second target group is VCs, who make VC-related decisions for INVs under conditions of great uncertainty in foreign environments and who understand what motivates entrepreneurs to strive for success during the process of new venture internationalization. Finally, for policy makers, this study offers insight into the important role they play as referrals in helping INVs successfully raise venture capital and work with VC firms toward new venture internationalization. This study can help policy makers gain awareness of the actions they can take in the future to contribute to a successful INV/venture capital relationship.

Entrepreneurs

This study offers several suggestions for entrepreneurs who aim to raise venture capital for new venture internationalization. First, the entrepreneur should be active in the local community to obtain appropriate referrals to VC firms. Appropriate referrals especially include angel investors and business support organizations that provide incubating services. These referrals can help achieve “match” and “fit” between the INV and VC firms, because they know both of them well before making introductions. Referrals can also accelerate the VC firm’s evaluation process by increasing the perceived value of an INV through implied trustworthiness.
Second, it is advisable to demonstrate entrepreneurial abilities in the internationalization process, such as having initial foreign customers, which can help gain the confidence of VC firms. If this is not attainable, the entrepreneur should approach the right VC firm that has international experience and network resources for assisting the INV in its internationalization process.

Third, although VC firms are opportunity-driven, an INV still stands a chance for investment even if the entrepreneur lacks internationalization experience and network resources. It is always worth the effort to start discussions and build relational capital as early as possible with VCs. At the very least, the INV can identify what areas of the company need improvement before investment can be obtained.

Fourth, showing willingness to cooperate increases the chance of being invested, because VC firms will monitor the business progress during post-investment activities. Fifth, the entrepreneur’s expectation of value-added services from VC firms should be realistic and based on the size, experience, and network resources of the VC firms. Too great an expectation can destroy relational capital in the collaboration stage if the expectations are not met. In truth, VC firms cannot always provide everything an INV needs for internationalization.

For entrepreneurs currently working with VC firms, the first suggestion is to continue developing relational capital and maintaining a pleasant relational atmosphere in which open discussion and information exchange can be achieved, so that adjustments in behavior can be made by both parties and common goals identified. The second suggestion is to maintain relational capital while finding an appropriate working approach that fits both entrepreneur and VC firm, which helps appropriate extra value from both parties. The final suggestion is to build upon, develop, and act on the existing relational capital. This can be of benefit for working with current or new VCs during following rounds of investment, or in the next venture.

Venture capitalists

This study provides advice for VCs who intend to invest in INVs. First, having effective relational capital within the local community increases the chance of obtaining a highly qualified deal flow through appropriate referrals. Referrals’ knowledge of both INVs and VC firms allows them to recommend INVs that fit a given VC firm’s industry and portfolio. With appropriate referrals, time and money spent on evaluation of INVs can be reduced.
Second, VCs should carefully evaluate INVs by considering the ability of the entrepreneur to control liabilities and risks inherent in new venture internationalization. This can be accomplished, in part, by paying attention to the relational capital the INVs have established around the business community. Third, VCs should pay particular attention to the valuation of the INV and strive for a balance of power between INV and VC firm. This approach preserves the sense of psychological ownership for the entrepreneur when he is able to continue exercising control of the INV after signing the venture capital investment agreement. In the relational capital formation process, VCs should avoid creating affective conflicts with the entrepreneur and try to maintain a pleasant relational atmosphere in which open discussion can occur. In the post-investment stage, VCs should offer greater flexibility to entrepreneurs engaged in international business, because this type of business is surrounded by greater uncertainty. VCs should provide not only capital and valuable advice, but also emotional support and patience, especially when the entrepreneur encounters industry- or external environment-related challenges. VCs should also adopt a proactive approach to having frequent interaction and communication with the entrepreneur to understand the specific interests of the entrepreneur. By increasing the level of trust within a congenial relational atmosphere, ROI can be secured by successful exit from the INV.

Policy makers

External environment surrounds INVs and VC firm is found to be important according to the empirical results. First, policy makers should create a healthy business ecosystem that promotes and facilitates entrepreneurial activities, provides support for INVs’ internationalization processes, and reduces the obstacles to INVs’ and VC firms’ signing of investment agreements. Second, governmental support organizations are trustworthy partners for both INVs and VC firms. As such, the advisors from public business support organizations should actively assist in INVs’ initial fundraising activities through their established investment networks – which are not necessarily limited to venture capital. Obtaining any kind of investment, whether from angel investors or third parties, creates a signaling effect that increases the credibility of the INV and its ability to raise venture capital. Policy makers should also create an hospitable environment for VC investors, particularly for attracting foreign VC firms, as the study results
have shown that foreign VC firms may bring more benefits and value-added services for new venture internationalization.

7.4 Evaluation of the study

Reliability and validity are two major criteria for evaluating quantitative research. Reliability refers to demonstrating that if the research is repeated, other researchers can achieve similar results and findings. Reliability is about whether the result is replicable. Validity refers to whether the means of measurement are accurate and can measure what the researchers intended to measure. Although reliability and validity have their roots in the positivist paradigm for accessing quantitative studies, they have wide application to qualitative work while designing a study, analyzing results, and judging case study rigor (Eisenhardt 1989b, Gibbert et al. 2008, Patton 2005, Yin 2003). However, discussion of validity and reliability requires substituting new terms for words to reflect interpretivist conceptions (Seale 1999: 465). Qualitative researchers often adopt quality, rigor, and trustworthiness in describing reliability and validity for qualitative studies (Davies & Dodd 2002, Golafshani 2003).

In the positivist paradigm, internal validity, construct validity, external validity, and reliability are the well-established tests for evaluating reliability and validity of quantitative studies. In the realist, critical realist, and constructivist paradigms, credibility, transferability, dependability, and confirmability are the corresponding tests applied for evaluating trustworthiness of the qualitative work (e.g., Denzin & Lincoln 1994, Lincoln & Guba 1995, Miles & Huberman 1994, Patton 2002, Silverman 2006, Yin 1994). In this study, the trustworthiness of a case study is evaluated by examining credibility, transferability, dependability, and confirmability.

Credibility corresponds to internal validity. Credibility checks whether the inquiry was carried out in a proper way. Use of triangulation techniques during the data collection and analysis phases enhances credibility (Lincoln & Guba 1995). Credibility can be achieved through collecting multiple sources of evidence in the data collection phase (Gibbert et al. 2008) and careful documentation of transcripts and field notes for cross checks. This study collected data from multiple sources, including primary interviews and presentations, as well as Internet documentation as secondary data for analysis.

The multiple case study method, which allows cross-case analysis, was chosen for conducting the empirical study. A qualitative analysis software, Nvivo, was
adopted to visualize the data and assist building causal relationships between key themes. In addition, this study has been presented to and reviewed on a regular basis by peer reviewers (Lincoln & Guba 1995).

Credibility also relies on the ability of the researcher who carries out the research (Eriksson & Kovalainen 2008: 294). An extensive amount of reading of articles from existing literature about the relevant topic, together with intensive interviews, increased the confidence of the author as researcher in making the claims for this study, based on a well-documented chain of evidence.

Confirmability is closely linked to construct validity. Confirmability assesses whether interpretation of data follows the logic and unprejudiced manner (Miles & Huberman 1994) and leads to an accurate observation of reality (Denzin & Lincoln 1994). Confirmability can be enhanced by describing research design and methods in detail. Chapter 4 described the choice of philosophical standpoint and detailed information on accomplishing a multiple case study. Confirmability also refers to the degree to which the findings can be easily understood and confirmed by others (Lincoln & Guba 1995). Chapter 5 analyzed the empirical data and selected quotes from interviewees to confirm the arguments of this study. When describing findings, tables and figures have been used to visualize the results and illustrate the causal relationships between key factors shown in Chapter 5. This study has been presented to the internal seminars organized in the department, where the confirmability audit has been involved to improve the quality of the work (Lincoln & Guba 1995), change the unclear aspects (Yin 2003), and make the arguments easy to understand.

Transferability is similar to external validity or generalizability. Transferability refers to the degree of similarity between current research and existing theory (Lincoln & Guba 1995) and whether the findings from one study in one context can apply to other contexts (Myers 2013). The purpose of transferability in qualitative studies is to achieve analytical generalization, and it intends to build theory from empirical data instead of statistical generation to a population (Yin 2003).

The abductive reasoning used in this study focuses on interplay between theory and empirical data. Due to continuous discussion between theory and empirical data, it allows the researcher to find a closer link between the current research and previous discussions on the topic. Furthermore, the empirical findings are reflected to the previous literature in Chapter 6 and 7 when discussing the research findings. As a result, a conceptual model has been developed to present the current research results by taking both the theoretical model developed in Chapter 3 and the empirical model constructed in Chapter 5.
Dependability is related to reliability in quantitative research. This study has been carefully designed by revisiting theory and data in a back-and-forth manner. This study has developed a case study protocol by carrying out the initial fieldwork as a pilot study, to test the questioning and its structure. Based on the pilot study, the research topic and questions were refined (Eisenhardt 1989b, Yin 2003). The interview questions were developed based on the pilot study by using semi-structured interview strategies. All of the interviews were digitally recorded, transcribed into text, and stored on a computer (Silverman 2006). Each step of the empirical research process was well documented in Chapter 4, followed by an empirical analysis in Chapter 5.

Goetz and Lecompte (1984) suggest that the researcher should take theory and ideas into account throughout each research phase. This study has taken the theoretical model as an *a priori* model to guide the research direction and later compared it with a constructed empirical model. Based on the theoretical and empirical models, as well as reflection to the existing literature, the conceptual model for financing entrepreneurial INVs has been elaborated to present the findings for this study.

### 7.5 Limitations of the study

A clear understanding of the limitations of research improves the quality of a study. There are a couple of theoretical limitations to this study. This study only focused on discussing the network relationship and early internationalization in INV literature. In VC literature, this study emphasized the process of relational capital formation and utilization between INVs and VC firms and did not deal with financial calculations on valuations and IPOs, if any. The scope of the study was the VC investment process. Activities of the INVs before raising venture capital and after exit were not taken into account.

Methodological limitations have also been found in this study. Few informants were interviewed from the five selected INVs, and there was an incomplete data source on the VCs’ side. This limitation resulted from the small number of founders and key employees present within six years of inception. The number of people who were involved in forming and utilizing relational capital with VC firms was rather small. In a typical case, only the founder was involved in the fundraising process with VC firms. In retrospective cases, some of the VCs who were involved in negotiating with case companies had left their jobs with the VC firms. The empirical data for this study was strongly focused on the entrepreneurs’ viewpoint.
and only gathered VCs’ views as supplementary comments. In particular, the focal point of utilization covered only the benefits the entrepreneur could obtain through the relational capital building process. The empirical data shed light on the differences between receiving domestic and foreign venture capital and each type’s approach to nursing INVs. However, the data was not strong enough to draw conclusions on the basis of the specific types of venture capital in terms of foreign or domestic, round of financing, size of investment, and its consequence for INVs. It is arguable that a foreign VC firm adds services that are more valuable for new venture internationalization, as shown in the Placing case. Moreover, a foreign VC firm can increase the likelihood that a portfolio company will list on a foreign exchange market, because connections to top-tier lawyers, investment banks, and accountants may be one of the mechanisms through which foreign VCs can facilitate international listing and thus overcome the liability of foreignness (Humphery-Jenner & Suchard 2013).

This study placed an emphasis on the relational capital building process between INV and VC firms for the purpose of new venture internationalization. However, the concrete outcomes for new venture internationalization that resulted from relational capital between INV and VC firms were somewhat vague. This research might serve as a pilot study for a quantitative survey to determine relational capital–related outcomes for new venture internationalization in more detail by focusing on post-investment interactions between INV and VC firms.

This study did not distinguish private VC investors from corporate VC investors. The concept of venture capital means different things to entrepreneurs and VCs. Particularly in Placing’s case, the entrepreneur considered U.S. and Finnish family-owned VC firms as angel investors, but the U.S. investor positioned himself as a venture capitalist.

### 7.6 Avenues for further study

Several research gaps have been identified while conducting this study. This study strongly focuses on entrepreneurs’ perspective on relational capital and the benefits INVs have received from VC firms. Further investigation could explore VCs’ understanding of relational capital formation and utilization, and determine what outcomes, other than financial ROI, can result from relational capital. In this sense, it is important to recall that most of the entrepreneurs interviewed for this study indicated that “relational capital is a two-way process.”
VC firms hold greater power than entrepreneurs do in the venture capital negotiation process, because the entrepreneur depends on the VC firm’s funding to survive and develop (Donaldson & Davis 1991). Therefore, there might be a concern that forming relational capital that facilitates information exchange will further decrease the negotiating power of the entrepreneur, especially if VC firms take advantage of information obtained from entrepreneurs through building relational capital with INVs during negotiation meetings. This is an interesting research gap on the entrepreneur’s power (Lehtonen 2006) in relation to VCs in the negotiation process, and how entrepreneurs can manage their power while developing relational capital with VC firms.

The behavior-related factors emerged from the empirical data as important for influencing the relational atmosphere and relational capital utilization in post-investment activities. Ojala and Heikkilä (2011) have also found that the entrepreneurs of Finnish new ventures feared losing control over their firms as an increasing number of Finnish new ventures have been financed by VC firms. Because their behavior, such as that driven by fear of losing control over INV, the entrepreneurs’ perceived emotional feelings, and their sense of psychological ownership, strongly influence collaboration between the INV and VC firm, there is room to explore the dyadic entrepreneur/VC firm relationship from a behavioral science perspective, including its influence on post-investment activities.

This study has indicated that relational capital played an important role in post-investment activities, but with the current dataset, this study has not been able to figure out exact outcomes directly resulting from the relational capital formation process. Further study efforts could be made to identify relational capital outcomes for INVs, such as how the relational capital of VC firms has accelerated the internationalization process of INVs. This study has suggested that foreign VCs add greater value to INVs, but there has not been enough empirical evidence to support this view firmly. Therefore, it would be interesting for further studies to explore and compare the value-added services that domestic VC firms add to INVs with those added by foreign VC firms. As the study results have indicated that the foreign VCs have been reluctant to establish relationships with distant INVs because of monitoring difficulties, it is also worth studying how INVs and foreign VC firms form, develop, and manage relational capital, and how foreign VC firms manage monitoring of the progress of INVs and help INVs with early internationalization.

This is a theory-building study based on a multiple case study method and can serve as a pilot study for understanding the role of relational capital in the INV/VC...
firm relationship. From a methodological perspective, a quantitative study can follow to verify the arguments and the conceptual model developed in this study.

### 7.7 Research summary

This study fulfills the purpose of examining the formation and utilization of relational capital for new venture internationalization between INVs and VC firms. I find this topic interesting because entrepreneurship has emerged as an important means of boosting economic growth in the City of Oulu during the last five years. The initial and inevitable step for new venture success is to obtain financial support for development. Venture capital investment that focuses on high-technology industries and high-risk ventures would be an ideal option for the startup phase of inexperienced technological ventures. A common consensus is that VC firms bring not only cash, but also valuable contacts and management know-how to their invested ventures. As a researcher, I have noticed that relationship plays an important role in obtaining such funding and in scaling up an INV after venture capital allocation. Therefore, I decided to explore it in-depth to understand the importance of relationship from both entrepreneurs’ and VCs’ perspectives.

This dissertation discusses the concept of “relational capital” and observes the interactions taking place between INVs and VC firms. Unlike much other research devoted to identifying social-relational capital as a mechanism to build resources around INVs, the aim of this study is to capture how INVs have developed early internationalization processes along with building up and utilizing relational capital with their financial resource-provider VC firms.

The work started with a systematic literature review. Chapter 2 discussed the INV, network, and venture capital literature closely related to my study. The reviewed literature was further discussed and criticized for framing a theoretical model. Chapter 3 introduced the key concept of “relational capital” and identified the important factors involved in relational capital by following the process of entrepreneurs and VC firms building and utilizing relational capital within the venture capital investment process. As a conclusion to the literature review, a theoretical model grounded in the INV, network, and venture capital literature was proposed to explain the relational formation and utilization in the venture capital process for new venture internationalization.

Qualitative and multiple case studies have been used to understand the phenomenon in-depth. Altogether, entrepreneurs from five case companies and VCs have been interviewed, creating an interesting data set for my study. Both
entrepreneurs’ and VCs’ viewpoints were taken into account to capture the entire picture. The empirical analysis started with capturing the relational capital formation and utilization process between INVs and VC firms for new venture internationalization via individual cases, along with potential consequences resulting from relational capital. The entrepreneurs’ individual thinking and efforts toward building relational capital were described. Moreover, when critical relational milestones (e.g., incidents) occurred, the impact on the feelings of the entrepreneurs and the INV’s relational tendencies were further documented.

VCs’ collective thinking toward relational capital and its benefits was summarized. The empirical study discussed and compared the two views of entrepreneurs and VCs on key constructs identified in the theoretical model. Individual cases were also compared, contrasted, and properly analyzed. Emerging issues such as external environment, human factors, and opportunity were added to the theoretical model. The empirical data concluded with an empirical model grounded in the data, which provides a new means of understanding the relational capital formation process between INVs and VC firms for new venture internationalization.

In the discussion section, by comparing the differences between the theoretical and empirical models, a conceptual model was developed as an outcome of this study. It provides insights for entrepreneurs who want to attract venture capital and for VCs who desire to work with INVs. According to the conceptual model, relational capital is an isolating mechanism that differentiates INVs from competitors. It achieves advantage and plays an important role in increasing the likelihood of being funded. More specifically, by mapping relational capital in each stage of the venture capital decision-making process, the research results showed that relational capital enables entrepreneurs to gradually tap into VCs’ networks in the deal origination phase and understand their investment policies in the screening phase. Relational capital embedded in founder increases the potential for visibility of the INV in the market and the likelihood of being acquired by a larger company. The ability of the entrepreneur to mitigate the liabilities of internationalization and decrease setup costs in foreign markets reduces the cost of venture capital funding. Visibility of the INV in foreign markets enhances the exit potential for the VCs. These effects contribute during the deal evaluation phase in the venture capital decision-making process.

During the relational capital formation process, a relational atmosphere is created between the INV and VC firm. The two parties find an appropriate approach to work together that fits each party and maximizes the value and effort of each
party for new venture internationalization. The relational capital increases the level of trust and mutual understanding, which enables the resolution of goal incongruence by applying agency theory to view this dyad relationship.

The research results also showed that maintaining ongoing relational capital helps in the process of raising later rounds of investment from the current VC firm. It also brings additional support, such as emotional support, for entrepreneurs who face difficulties and challenges in uncertain foreign markets or industry downturns. A congenial relational atmosphere creates an open communication environment between entrepreneurs and VCs that facilitates information sharing and exchange. The research results also represent the worst-case scenario of relational failure: replacement of the entrepreneur as CEO and ultimate venture failure.

Generally, the relational atmosphere influences the overall internationalization performance of the INV after allocation of venture capital. As a final conclusion for INVs and VC firms, it is worth building a congenial relational atmosphere in which the INV and VC firm can work closely together.
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216


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Appendix 1 Example of categorization and linking of codes, categories and theme: Relational capital formation
Appendix 2 Example of categorization and linking of codes, categories and theme: Relational capital formation
Theme

Emerging categories

- Appropriate working approach between INV and VC firms
  - Never give up
  - Haven't sold the company with lower price
  - Continuous funding
  - Patience to wait

- Emotional support from VC firms
  - Only financial support
  - Motivation
  - Sweat equity

- Value appropriated from entrepreneurs
  - Information/saving time and monitoring costs
  - Open discussion

Emerging codes
Appended Example of categorization and linkage between codes, categories and theme: Relational capital atmosphere

<table>
<thead>
<tr>
<th>Codes</th>
<th>Chaining/E</th>
<th>Sending/E</th>
<th>Placing/E</th>
<th>Viewing/E</th>
<th>Basing/E</th>
</tr>
</thead>
<tbody>
<tr>
<td>Perceived relational capital after VC</td>
<td>Not satisfied, decide not to quit raising VC</td>
<td>Appreciate for workshop type of discussions, satisfied with VC business expertise, having power in negotiating valuation</td>
<td>Smooth and open discussions, not value us low</td>
<td>Good in first two rounds, no trouble or conflicts with VC firms.</td>
<td>Surprised in valuation</td>
</tr>
<tr>
<td>Subcode: positive</td>
<td></td>
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<td>(Sending, Placing, Viewing in first two rounds)</td>
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<td>Subcode: negative</td>
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<tr>
<td>(Chaining, Viewing in the third round, Basing)</td>
<td></td>
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<tr>
<td>Emotion feelings after VC investment decisions</td>
<td>Not pleasant Satisfied Appreciate Satisfied</td>
<td>Changing the feeling as employees become employees, however, disappointed</td>
<td>Afraid to negotiate, want money, employees</td>
<td></td>
<td></td>
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<tr>
<td>Subcode: satisfied</td>
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<td>Subcode: unsatisfied</td>
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Fan Wang

FROM RELATIONAL CAPITAL TO VENTURE CAPITAL

FINANCING ENTREPRENEURIAL INTERNATIONAL NEW VENTURES