Discussion Paper

Exploring the difference in performance between UK/European venture capital funds and US venture capital funds

(Interviews with venture capitalists and other stakeholders in UK/Europe and USA)

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Preface

There is a long-standing difference in performance between European and US venture capital funds. This has led to reduced allocations of funds raised for European venture from non-governmental sources, such as the traditional institutional investors, and consequently less finance available for investment into high-growth entrepreneurial companies in Europe.

So what explains this performance difference? Are US VC firms simply better at investing in potential high return investments? Recent studies have not fully explained the performance gap between European and US VC funds, attributing some of the difference to serendipity and “unmeasured or unmeasurable” factors.

Whilst working in my former career at PwC, I became intrigued with the apparent under-performance of European venture capital funds compared to their counterparts in the USA. My responsibilities at PwC included working with the BVCA on the association’s annual performance measurement survey which consistently revealed an overall underperformance of venture capital funds in the UK compared to the USA, as did Invest Europe’s data for Europe as a whole.

I decided to undertake research, under the supervision of Professor Colin Mason at the Adam Smith Business School, University of Glasgow, to investigate the difference in performance between UK / European and US VC funds. I conducted a series of in-depth interviews with venture capitalists from 64 different VC firms from both sides of the Atlantic. I supplemented my VC interviews with 40 further interviews with people ancillary to the industry, including limited partner investors, entrepreneurs, VC-related individuals, advisors to the sector and corporate venture capital firms. My work, whilst entirely independent and self-financed, has had the support and encouragement of the BVCA’s Venture Capital Committee.

The principal findings of my research are the subject of this report. A key purpose of the report is to communicate to institutional investors that the UK / European environment for venture capital is improving and, as UK VC firms adopt more best practices (some of which are based on those of the US VC firms sampled in this research), the performance of UK / European VC funds should continue to improve encouraging increased institutional funding for the sector. The report includes practical implications and recommendations for sharing of best practices.

I hope that this report generates discussion and debate by the VC industry, by LPs and by entrepreneurs. I look forward to carrying out follow-up work on further developments in the industry.

Keith Arundale
Doctoral Researcher, Adam Smith Business School, University of Glasgow

May 2017
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The views expressed in this paper are those of the author (and of course the interviewees!).

Keith Arundale

Keith Arundale is a Doctoral Researcher at the Adam Smith Business School, University of Glasgow where he is carrying out research into the difference in performance between European and USA venture capital funds. He is also a Visiting Fellow at the ICMA Centre, Henley Business School, University of Reading where he teaches private equity & venture capital to postgraduate and undergraduate students. Keith is a chartered accountant and a chartered marketer and was formerly with PwC where he led the venture capital and marketing programmes for the Global Technology Industry Group in Europe. He is the author of “Raising Venture Capital Finance in Europe” (Kogan Page, 2007) and the BVCA’s “Guide to Private Equity” (2010).

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Introduction

The aim of this report is to: (1) investigate the historic difference in performance between UK / European and US VC funds by interviewing venture capital investment executives and other stakeholders on both sides of the Atlantic as to VC investment practices and the wider environment in which VC funds operate and (2) to encourage discussion and debate about best practices that could be adopted by UK / European VCs, some of which are based on the investment practices of US VCs as reviewed in this study.

UK and continental European venture capital (VC) funds have historically performed worse than US VC funds. The gap in performance has narrowed since the collapse of the dot.com/internet era of 1999 to 2001 but there is still a significant difference in performance. This has led to reduced allocations of funds raised for European venture from non-governmental sources, such as the traditional institutional investors. This, in turn, could result in a shortage of VC funds going forward for investment into young, innovative, potentially high-growth European companies, notwithstanding increased activity by alternative sources of finance in the early stages of the funding escalator such as crowd funding and business angels.

Whilst previous research in the area of venture capital fund performance and investment practices has largely involved the use of regression analysis on large data sets or a questionnaire approach this research adopts a qualitative approach of semi-structured interviews with executives from 64 separate VC firms in Europe and USA. It also investigates for perhaps the first time in an extensive, qualitative manner, the entire investment process from sourcing deals to exiting deals, specifically contrasting Europe and the US in the context of fund performance.

In addition to the interviews with VC practitioners, the opinions of interested, non-practitioner, participants in the European and US venture capital sectors were sought as to the reasons for the performance difference between European and US VC funds. Some 40 non-practitioners were interviewed in this study, including limited partner investors in venture capital funds, entrepreneurs in receipt of venture capital financing, former venture capital firm professionals, venture capital firm executives ancillary to the investment role, venture capital professional body executives, advisors to the industry, corporate venturing investment executives and others who are deeply involved in the industry. Few studies have ascertained the views of non-VC practitioner experts. The report contrasts the views of practitioner and non-practitioners in the venture capital industries in Europe and the US, perhaps the first time that such a comparison has been done for a relatively large qualitative sample. Many verbatim comments from VCs and others are included throughout this report.

The study seeks to ascertain if there are generally agreed factors that may give rise to the performance difference between European and US venture capital funds for the sample of firms investigated in this study. Potential factors may be of three types. First, they may be structural, resulting from characteristics of the funds themselves, for example the size of the funds, their strategic focus or the backgrounds of the investment executives who manage the funds. Secondly, they may be operational such as the investment practices of the VC firms which manage the funds. Thirdly, they may reflect wider environmental factors such as culture and attitude to risk and the wider ecosystem in which the funds operate. Establishing a unique dataset from a thematic analysis of the transcribed interviews the study found
structural and operational differences and contrasts in the approach to investing between US and European funds.

This report considers in particular whether differences in the investment practices of the European and US VC firms that manage funds for investment, and differences in the environments in which they operate, could at least in part explain the difference in performance between European and US funds. The principal findings of the report were presented by the author at the 2015 and 2016 annual conferences of the Institute for Small Business and Entrepreneurship (ISBE) (Arundale, 2015 and 2016). By adopting some of the investment practices of the US VC firms included in this study and more of an open, sharing culture, European VC performance could potentially be improved. This could lead to increased investment in the asset class and more funds for entrepreneurial activity going forward.

“I think the value in your effort is if you can begin to emerge with a vision for what needs to be done for early stage in Europe. There is no real value in analysing the past and highlighting some differences and so on and so forth. There is real value if you analyse the past and say “what lessons have we drawn and where do we go from here?”” (UK VC related interviewee).
Executive summary - Principal findings and areas for discussion

This research investigates whether differences in practice between the ways in which European and US venture capital funds go about originating, executing, monitoring and exiting from their investments, and the structural and wider environments in which they operate, might go some way to explaining the historical difference in performance between European and US VC funds.

Semi-structured interviews were carried out with VC practitioners from 64 firms across UK, continental Europe and US, supplemented with 40 interviews with limited partner investors, entrepreneurs, advisors and corporate venturing investment executives. Thematic analysis was used to identify emergent themes.

For the sample of VC firm executives and other participants interviewed in this study a number of differences were found between UK / European and US VC firms and the structural, operational and wider environments in which they operate, as summarised here:

Structural

- Smaller size of funds in Europe compared to the US. US funds in the sample had an average size of $282m, compared to UK funds with average size of $168m and continental European funds of $128m. There is a shortage of finance, particularly of later stage finance, for growing and scaling companies in Europe.

  “There’s a massive inefficiency in the UK because you haven’t got scale of funds; you’re forever having to look to raise another round of funds and then another round of funds and at each break point for the next fundraising, there are valuation disputes, there are allocation disputes, it’s just hugely inefficient, a huge drain on management time”. (UK LP)

- Differences in the backgrounds of the VC investment executives. US VC firms had proportionately more partners with operational and, to a lesser extent, entrepreneurial backgrounds. European VC firms had a greater proportion of partners with a financial, investment or consultancy background.

  “People who are good entrepreneurs are often the folks who end up becoming venture capitalists here”. (US Entrepreneur)

- US firms have around one more partner in total than European firms and more US firms have two partners working together on a deal at the same time.

Operational

- US VCs were consistent in using a “theme” approach to identify future areas for potential investment. European VCs tended to follow the trend.

  “About 10 times per year partners decide where to put resource to try and identify an investment thesis, whatever it takes, and present to everyone in the group a thesis with respect to, is there an investable idea behind that?” (US VC)
- More US VCs pursued a home run, higher risk, “1 in 10” investment strategy than European VCs, perhaps due to the intensively competitive environment in which US firms operate where taking a middle ground approach does not work, compared to Europe where there are constraints with funding and scaling. The more recently established VCs in UK do appear to follow more of a US higher risk approach.

“When we speak with one of our LPs in particular I mean their constant push is “are you taking enough risk in your portfolio?” (UK VC).

- The brand strength of US VC firms, particularly those in Silicon Valley, aids quality deal flow and optimal exits through relationships with big corporates.

“I can't think of European VC backed firms that would have the same kind of brand franchise for a start-up that would be as attractive as some of the Silicon Valley groups here in North America”. (US LP)

-Whilst most US VCs in the sample reached investment decisions unanimously or by consensus, a senior partner could force (“railroad”) decision in some US VCs. Consensus may “kill” the outlier deals which may produce outlier returns.

“What we found was that consensus would kill the outliers. Anybody who feels strongly about something can make it happen”. (US VC).

- Use of more entrepreneurially friendly terms in investment deals in the US, particularly on the West coast, versus investor friendly terms in Europe, again perhaps reflecting the more competitive environment in the US, particularly in Silicon Valley and perhaps an entirely rational approach to protecting the downside in Europe.

“Europeans are saying how do I not lose and Americans look at the question how do I win?” (US Silicon Valley VC)

- Perhaps greater use of milestone based financing / drip-feeding by European VCs.

“American CEOs think that European VCs just want to drip-feed them; the European VCs under-capitalise companies”. (US Silicon Valley VC)

- US VCs focus on the metrics portfolio companies need to manage in order to determine how much money to continue to invest at subsequent rounds.

“The US VCs know exactly what metrics they’re willing to fund. The reason they’re willing to put another X in is because they’ve seen that happen before”. (UK CVC)

- European VCs syndicate with other VCs often for monetary reasons. US VCs may not need additional finance but collaborate together to pool expertise and know-how.

“We syndicate not because we need to (we have the ability to write the whole cheque if we wanted to) but because we want to”. (US VC)
- More US VCs wait for the best exit. There was a tendency, perhaps, in Europe to exit from investments too early, possibly because of pressure from institutional investors to demonstrate returns.

“You’ve got to take the best offer on the table for the money that you’ve got so you’re maximising your return within the capabilities you have of limited fund sizes and that is a big issue for the UK”. (UK LP)

- Though in Europe VCs may keep poor investments going for longer.

“In the UK, with smaller funds, the proportion of the fund of each investment is going to be larger and, therefore, there’s going to be greater reluctance to walk away and admit you got it wrong”. (UK LP).

**Wider environment and other factors**

- Cultural differences between Europe and the USA, including a greater propensity for risk in the US and not thinking “big” enough in Europe.

“There are just as many smart people with good ideas in Europe. I think there’s only just a lack of entrepreneurial capital and mindset”. (US advisor)

- Relative lack of experienced CEOs and serial entrepreneurs in Europe compared to the US.

“I think Europe is getting there but we didn’t have that initial, we don’t have that large enough base, yet of entrepreneurs and CEOs that have done it before”. (UK CVC)

- Difficulty of scaling by investee businesses in Europe, largely due to a relative shortage of funds and the fragmentation of the European markets.

“The challenge for Europe has always been that we don’t have big enough home markets to build great home run returns, so companies need to be international from day one”. (UK VC)

- Difficulty with copyright law in Europe.

“Whilst there is now a unitary patent system and copyright across Europe the issue is who licenses it for which territory. This puts off US VCs from investing in the UK”. (Patent expert at Silicon Valley based company)

- Difficulties of exiting in Europe with less receptive stock markets and poorer connections with large corporates.

“You don’t IPO your company in London unless there’s something wrong with it usually. Because it’s not an exchange that’s gonna value a high tech company”. (UK CVC)

- An open and sharing approach in the US, with a willingness to share contacts, talents and information, contrasted with a more proprietary, protectionist, hierarchical approach in Europe. Silicon Valley was specifically highlighted with its unique open, networked ecosystem.
“This country is a lot more philanthropic. People feel they want to give back and that runs through the whole Valley. People are much more protective in Europe. (US Advisor)

- Importance of technology clusters for growing companies, particularly the open but tightly networked ecosystem of Silicon Valley.

“The investments, the CEOs and their teams are just surrounded by a phenomenal ecosystem (in Silicon Valley). The connections are just phenomenal: connected advisers, connected partners. The Valley is just unique” (UK VC).

For discussion

There are many excellent features about the UK / European VC sector. There is generally an adequacy of capital for early stage investment, including VC, business angel and crowdfunding finance, many accelerators to assist high-growth businesses, the formation of the British Business Bank, a higher number of interesting companies coming through for series A and B investment, much technological innovation from outstanding universities, centres of excellence in artificial intelligence, fintech and many other areas and exciting initiatives for digital businesses such as Tech City UK. There are more and more students studying entrepreneurship and joining entrepreneurial companies and the more recently established UK VC firms are operating along US Silicon Valley lines in terms of the entrepreneurial backgrounds of their partners and the higher risk approach to investing.

Whilst the UK / European VC environment is improving, overall VC fund performance remains better in the US than in UK / Europe. This was borne out by the available performance data for the VC firms included in this study. In order to replicate the success of US VC funds, European VC funds could consider raising larger funds, where practical and possible, for follow-on funding and scaling, embracing a “theme” approach to identifying hot areas for investment, pursuing more of a “home run” investment strategy where considered practical and rational, a less proprietary approach to deals with more networking and sharing of information and best practices, building collegiate syndicates and a focus on data and metrics that drive investment decisions.

In addition there is the need for more receptive public markets for technology companies and more government support and incentives for clusters with more technology R&D taking place via government and military sponsored research.

A key aim of this report is to encourage debate and discussion on these areas and on the constraints to their practical implementation. By sharing and adopting best practices (some of which may be based on those of the US VC firms included in this research) the performance of UK / European VC funds should continue to improve encouraging increased institutional funding for the sector. This could lead to improved opportunities for financing the potentially high-growth companies of the future in Europe.

Readers are encouraged to submit their comments to the author of this report at: keith@keitharundale.com.
Background

There is a long-standing historic difference in performance between European and US venture capital (VC) funds. VC fund returns pooled over the period 1991-2007 were on average 6.9% per annum for Europe and 18.9% per annum for US (Clarysse et al. 2009). Earlier studies by Hege et al. (2003) and Megginson (2004) revealed that US VC funds generally report significantly higher IRR performances than their European counterparts. The latest performance data published by Invest Europe (formerly the European Private Equity & Venture Capital Association) prepared by Thomson Reuters showed that the 10 year returns for VC funds were 5.03% for the US but just 0.84% for Europe (EVCA 2014).

Looking specifically at UK fund performance compared to the US, research by Lerner et al. (2011) for Nesta indicated that the historic performance gap between the UK and the US was narrowing, with the average performance of funds raised pre-boom 1990 to 1997 being 12.71% for UK and 32.95% for US compared to -1.21% for UK and -0.21% for US for funds raised post-boom 1998 to 2005. However in a later report by Marston et al. (2013) for Nesta, the gap between UK and US was widening with the average IRR for funds formed between 1990 and 1997 being 13.98% for UK funds and 33.34% for US funds. For funds formed between 1998 and 2007 the performance was -0.53% for UK funds and 3.87% for US funds. Marston et al. (2013) explain that this recent better performance of US funds could be driven by a resurgence of successful technology IPOs in the US and lucrative trade sales to cash-rich giant internet companies.

As reported in the June 2016 edition of the ICAEW’s Corporate Financier magazine, US VC funds returned 21.5% in 2014, 18.0% over three years and 10.3% over 10 years (Cambridge Associates US Venture Capital Index) whereas UK VC funds returned 14.5% in 2014, 10.9% over three years and 4.6% over 10 years (BVCA Performance Measurement Survey, 2015).

These studies illustrate that European VC funds have consistently underperformed US VC funds which confirms the starting point for this research.

The performance difference between European and US VC funds has led to difficulties in raising new funds for European venture investments with reduced allocations of funds raised by European funds from non-governmental sources, such as the traditional institutional investors, ie the banks, insurance companies and pension funds, resulting in a shortage of funds going forward for investment into young, innovative, potentially high-growth European companies. Indeed, according to Invest Europe, overall funds raised for European venture of €5.3bn in 2015 were 36% less than in 2007. This has led to the European VC industry being more dependent on funds from government agencies, principally the European Investment Fund. Funds raised from government agencies for allocation to European VC in 2015 were 20.6% of the total funds raised for VC, up from 7.9% in 2007, with €1.1bn of government funds being raised in 2015 compared to €0.6bn in 2007 (Invest Europe Research, 2016). This percentage allocation by government agencies may well be understated. In another presentation of their data Invest Europe quotes a figure of some 31% for the allocation by government agencies to European venture in 2015; this is after extrapolating unclassified amounts across categories of investor. The EIF itself backed 45% of funds raised by European VC firms in 2014 (36% in 2007) with 12% directly attributable to EIF (5% in 2007) (European Investment Fund, 2016). Continued support from the EIF for UK venture funds may be in question following the Brexit decision.
There are many variables that can affect the performance of VC funds, including such areas as size of funds, track record of VC, strategy (investment stage, sector classification and geographic focus), timing and amount of VC financing provided, number of tranches of financing, capital inflow and vintage years, monitoring and control processes over portfolio companies, how VCs add value, syndication, skills / experience of the VC partners, valuation of unrealised investments, timing and type of exits, and the general economic environment.

Whilst many of the variables affecting VC fund performance have been subject to academic investigation (for example see Kaplan and Schoar 2005; Lerner, Schoar and Wong 2005; Diller and Kaserer 2005; SVB Capital 2010; Ljungqvist and Richardson 2003; Gottshalg et al. 2003; Aigner et al. 2008; Lerner et al. 2011; Schwienbacher 2008; Phalippou and Gottschalg 2007), there were only a relatively small number of studies that have sought to explain the reasons for the relative underperformance of European VC funds compared to US funds at the commencement of this research (for example, Hege et al., 2003 and 2009; Dantas and Raade, 2006). Subsequently, Lerner et al. (2011) in their work for Nesta found that various fund characteristics, such as year of formation of fund (vintage year), size of fund, investment stage focus, industry sector focus and fund manager attributes such as prior experience in the market and strategic choices such as number of companies invested in, amount committed, number of co-investors, do not explain the magnitude of the difference in performance between UK and US funds. Later research for Nesta (Marston et al., 2013) also concluded that fund choices and fund characteristics do not explain the performance gap for pre-1998 or post-2003 funds. It did however conclude that the UK has slower and less profitable exits which would certainly impact on performance.

Axelson and Martinovic (2013), in a report for the BVCA “European Venture Capital: Myths and Facts” conclude that venture capital backed exits in Europe and the US have the same determinants of success in Europe and US, with more experienced entrepreneurs and VCs being associated with higher probabilities of exit: IPO exits of deals from the same vintage year have equal success in Europe and US though Europe has a lower probability of exit via trade sales. Axelson and Martinovic (2013) state that a contributor to the difference in performance is due to serial entrepreneurs being less common in Europe. They also comment as previously mentioned above on European VCs having less experience than the US. They find no evidence of a stigma of failure for European entrepreneurs.

Other differences that have been postulated as contributing to the gap in performance between European and US VC funds include the difference in the contractual relationships between VCs and entrepreneurs, the superior screening abilities of US VCs, the greater sophistication and better use of networks by US VCs and syndication used more effectively by US VCs (Hege et al, 2003, 2009) and also the finding that European VCs are less “active” investors (Schweinbacher, 2008). Fund characteristics such as size, stage and sector focus do not explain the magnitude of the European / US performance gap (Lerner et al, 2011; Marston et al, 2013).

Wider environmental areas such as cultural differences (Marston et al, 2013) and serendipity and “unmeasured or unmeasurable” factors are mentioned as possible factors for the variation in returns between UK and US VC funds (Lerner et al 2011), but these have not been specifically investigated in the above research studies in the context of the performance difference. Several of the practitioners with whom the author has spoken mention “luck” as a key factor to success.
The relatively few studies that have specifically investigated the difference in performance between US and European VC funds do not either separately or taken together fully explain the reasons for the totality of the performance gap. The performance difference between US and European VC funds is therefore in need of further investigation in order to confirm whether there are additional structural, operational and wider environment factors, other than those already identified by previous studies, that are contributing to the performance gap.

The potential contribution of the research reported on here is to investigate, for perhaps the first time by using an extensive, qualitative approach, the entire investment process from sourcing deals to exiting deals (Tyebjee and Bruno, 1984), specifically contrasting Europe and the US in the context of fund performance and the wider environment in which the funds operate, in an attempt to explain the reasons for the performance difference.

**Methodology**

Embracing engaged scholarship (Van de Ven, 2007) with the researcher’s practical experience in the VC industry (gained during a working career with PwC), the approach taken in the research has been to carry out interviews of around one hour’s duration with senior VC practitioners and related stakeholders in both Europe and the US using a semi-structured aide-memoire approach. The researcher covers the entire investment process (origination, execution, monitoring and exiting) in the interviews (Tyebjee and Bruno, 1984). The interviews took place between September 2012 and September 2014 with the detailed analysis carried out in 2015 and 2016. Interviewees were assured of confidentiality; their names and their organisations are not disclosed in the report.

There are relatively few studies that have employed qualitative interview techniques to investigate VC fund performance and VC firm investment practices. The majority of the existing studies use quantitative techniques on large data sets applying regression analysis of variables and/or survey techniques involving questionnaires sent to a large number of participants for completion.

**VC interviews**

The VCs interviewed in this research form a purposive sample drawn from membership of professional VC associations and from the researcher’s and others contacts in the industry. The sample size of VC firms (64 separate firms) utilises the concept of saturation and also allows for the assessment of variation between the distinct VC groups in terms of geographical location. The VC firms were sourced from a cross-section of stage and sector specialisms as can be seen in Table 2. Half the VC firms were focused on early-stage ventures, the others invested across the venture stages with two firms focused on growth deals. Firms invested across the broad spectrum of IT and lifesciences, sometimes specializing in one or both of these sectors and sometimes having a narrow focus on specific areas, such as digital media.

Some 65 interviews (64 separate firms) were carried out with senior VC executives from 39 separate European and 25 separate US VC firms as follows:

**Europe:** UK 26, France 3, Germany 3, Ireland 3, Scandinavia 2, Spain 1, Switzerland 1
**US:** California 13, Boston 4, Pittsburgh 4 (5 interviews), Baltimore 1, Cincinnati 1, New Jersey 1, New York 1.
36 of the 65 interviews were carried out face-to-face at the VC firms’ offices or other suitable venues (the face to face interviews were held in London, Silicon Valley and Pittsburgh). The remaining interviews (continental Europe and elsewhere in US) were conducted over the phone.

All 65 interviews were transcribed and the typed transcripts reduced to 4 to 6 page outlines within theme categories as follows:

Theme categories:

- Size and vintage year of fund
- Geographic focus of VC fund
- Performance of VC fund
- Professional backgrounds of investment executives
- Deal generation
- Approach to due diligence
- Investment approval process
- Terms of investment / use of syndicates
- Monitoring and portfolio review
- Adding value
- Exit process
- Europe / US differences from the perception of the interviewee
- Reasons for success or failure.

Themes were developed using an inductive/data driven approach, reducing the raw transcriptions to a shortened outline form within categories pre-determined from prior research and following the aide-memoire used to conduct the semi-structured interviews.

The outlines of the transcribed interviews were further summarised onto an Excel spreadsheet. Categories were sub-coded for further themes. The spreadsheet categories were analysed for percentage of recurring themes.

Non-VC interviews

The non-VCs interviewed in this research form a purposive sample drawn from the author’s existing contacts in the VC industry, introductions and referrals from VCs, VC professional associations and UK Trade & Investment (UKTI) and contacts made through attendance at VC and corporate venturing conferences. The sample size of non-VCs (40 individuals each from separate entities) utilises the concept of saturation and also allows for a representative number of individuals from different categories of non-VCs, including limited partner investors, entrepreneurs, VC-related individuals, advisors to the sector, corporate venture capital firms and other individuals involved in the industry.

Some 40 semi-structured interviews were carried out with senior non-VC practitioners, comprising 19 from Europe (15 UK, 4 continental Europe) and 21 from the US. The interviews were held with 7 limited partner investors, 6 entrepreneurs, 7 VC-related individuals (including a senior industry figure and VC firm founder, executives of VC professional associations in Europe and USA, executives of a bank involved in lending to VC backed companies), 7 advisors to the sector, 6 corporate venture capital firms and 7 other individuals involved in the industry (including professors from a US technology university
and executives from a European stock exchange and a major US Silicon Valley technology company).

25 of the 40 interviews in this study were carried out face-to-face at the non-VC’s office or other suitable venues (the face to face interviews were held in London, Silicon Valley and Pittsburgh). The remaining interviews (continental Europe and elsewhere in US) were conducted over the phone.

All 40 interviews were transcribed and themes were developed using an inductive/ data driven approach. The raw transcriptions of the interviews were developed into 4 to 6 page outlines within categories pre-determined from the author’s research of VC practitioners as regards structural and operational investment practice areas and also with the wider environmental areas of economic, supply of VC finance, regulatory, fragmented markets, networks, ability to scale, stock markets, government support, technology hubs, overall culture and propensity for risk.

The outlines of the transcribed interviews were further summarised onto an Excel spreadsheet. Categories were sub-coded for further themes. The spreadsheet categories were analysed for numbers of recurring themes.

Limitations

Whilst the author’s studies of both VCs and non-VCs comprise some 105 interviews in total, which is certainly comprehensive for a qualitative study, the findings cannot be extrapolated to the full population of VCs or indeed non-VCs. Further work on the areas of potential difference highlighted above could be subject to more extensive sampling and quantitative studies, controlling for factors using regression analysis and this could narrow the range of characteristics that impact on the performance difference.

Whilst there were interviews with 13 separate VCs from continental Europe, with the non VC interviews continental Europe was somewhat underrepresented with only 4 non-VC practitioners interviewed. This could be extended in future investigations.

Principal findings

The principal findings of the research are organised into structural, operational and wider environmental categories, with the responses and views of the VC interviewees followed by the non-practitioner interviewees included for each variable within these three categories. The findings were discussed, and some practical implications considered, with members of the BVCA’s Venture Capital Committee in June and September 2016; their verbatim comments are included as appropriate (indicated with a “*”).

Initially in this section the data confirming the existence of a performance difference between the US and European funds included in the sample is discussed.

Confirmation of performance difference between European and US VC funds

The US VC firms in this sample had a greater number of funds with top-quartile performance and certainly outlier high performance than the European firms included in the sample. This
is consistent with the overall historic difference in performance between European and US VC funds as referred to earlier in this report.

Independent performance on funds from 26 of the 64 VC firms was provided on special request by an independent data provider. 15 of these firms had top-quartile performance for their most recent fund (US 7, UK 5, E 3); the number of firms for US, UK and continental Europe (E) are shown in the brackets. 19 firms had at least one fund where performance was top quartile (US 11, UK 5, E 3) and 12 firms had two or more funds with top-quartile performance (US 7, UK 2, E 3). In addition 6 US firms, but no UK or E firms had funds whose performance showed an IRR of >50%.

Independent performance data was also available from other data providers. 7 of these firms had their most recent fund with top-quartile performance (US 6, E 1), 11 firms had at least one top-quartile fund (US 10, E 1) and 7 firms had two or more funds with top-quartile performance (US 6, E 1). Additionally, 6 firms had funds with outlier performance >50% (US 5, E 1). The findings from these data providers support the first set of data. Only 3 firms showed consistency of top-quartile performance between all their funds (2 US and 1 continental European firm). Venture capital funds have generally been shown to have persistence in performance from fund to fund (Harris et al., 2014).

Firms were also asked about their own views on their performance. Of the 61 firms who responded 46% said that their most recent fund had top-quartile performance (US 60%, UK 32%, E 43%), 64% said that one of their funds had top-quartile performance (US 84%, UK 45%, E 57%) and 33% said two or more funds had top-quartile performance (US 48%, UK 27%, E 14%). This is consistent with the better performance of US funds shown by the independent sources noted above.

Whilst some US LPs had little experience of investing in European VC funds, 6 of the 7 LPs interviewed confirmed a performance difference between European and US VC funds (US 2, UK 3, E 1) with European returns being worse than US returns overall. This is consistent with the difference in performance from the VC interviews as noted above.

“I think probably the top deciles of VCs in the US would outperform the top deciles of VCs in Europe”. (US LP)

“The European portion of (our) venture portfolio was so small it was really unfair to compare the two. But, yes, I think as a rule the US has done better than Europe”. (US LP)

UK LPs had more experience of investing in US VC funds and confirmed the performance difference:

“We have incredibly high performing US venture experience. In Europe we have some okay performing and in both the US and Europe we’ve got some dreadful performing. The US is quite a broad spectrum from super high performing to super terrible. And Europe is a spectrum from terribly okay to super bad performing if that makes sense”. (UK LP)

Two LPs mentioned that the better performance of the US VC funds was due to outliers. There were also comments about the lack of consistency in the performance of European funds:

“The big outliers were in the US, the maximum performance, I think we found, was 720% IRR
as opposed to European 260% IRR. So, you can always find European funds that perform as well as some of the US funds but what I never managed to find was consistency of performance in European funds compared to the best US funds. So we had portfolios of US funds which would consistently turn in 30% plus IRR from the same management team and we never had a European fund that did it more than... well, a venture fund, I think I’d struggle to name any one that had done it twice, to be honest”. (UK LP)

Harris et al (2014) confirmed a persistence in the performance of US VC funds. There was a sectoral focus in the performance of VC funds; a UK LP believing that it is the IT sector, and software in particular, that is responsible for the better returns in the US:

“The stuff that is highly performing in the US is mostly software, it’s IT driven in the West Coast. East Coast healthcare stuff for instance in the US is no better than the European healthcare stuff, in our experience. But the only thing anywhere in the world in venture which has shone has been West Coast centric IT mostly software stuff”. (UK LP)

However Lerner et al (2011) and Marston et al (2013) concluded that fund choices and characteristics do not explain the magnitude of the performance gap. The difference in performance was also mentioned by two of the corporate VCs (CVCs) interviewed (US 1, E 1) with one referring to Thomson Reuters performance data and the other referring to their own portfolio where performance had been better in Palo Alto than in Europe.

An advisor interviewed referred to the historic performance data:

“I’m not pre-empting the outcome of the study but, I mean most of the published stats to date would suggest that Europe lags behind the US in terms of VC performance anyway”. (UK Advisor)

Structural differences

The research investigated the size of the funds included in the sample and the backgrounds of the partners, categorized as financial / investment, consultant, operational or entrepreneurial. As explained below, US VC funds in the sample were considerably larger than UK and continental European VC funds. US firms had around one more partner in total than European firms. They also had proportionately more partners with operational and, to a lesser extent, entrepreneurial backgrounds.

Fund size and follow-on financing

US VC funds in the sample with an average size of $282m were considerably larger than UK and continental European funds, which had average sizes of $168m and $128m, respectively. The largest US fund ($1,515m) was ~3 times the size of the largest UK ($557m) and continental European fund ($557m). The larger size of US funds is consistent with previous studies (Lerner et al. 2011) and would better permit US VCs to fund entrepreneurial businesses through to exit. However, larger size funds do not necessarily perform better than smaller funds (Gottshalg et al. 2003). In fact there is an optimum performance level around medium size funds ($84m to $365m) according to Lerner et al. (2011) as the very largest funds may not be as selective as more optimally sized funds in their selection processes.
Table 1: Size (and age) of VC funds in sample

<table>
<thead>
<tr>
<th></th>
<th>US</th>
<th>UK</th>
<th>Cont. Europe</th>
</tr>
</thead>
<tbody>
<tr>
<td># of firms with fund info in sample*</td>
<td>22</td>
<td>18</td>
<td>14</td>
</tr>
<tr>
<td>Av size of funds ($m)</td>
<td>282</td>
<td>168</td>
<td>128</td>
</tr>
<tr>
<td>Smallest fund size ($m)</td>
<td>12</td>
<td>15</td>
<td>11</td>
</tr>
<tr>
<td>Largest fund size ($m)</td>
<td>1,515</td>
<td>557</td>
<td>557</td>
</tr>
<tr>
<td># of funds before 2000</td>
<td>14</td>
<td>4</td>
<td>5</td>
</tr>
</tbody>
</table>

* an average size of fund was calculated for the funds pertaining to each of 54 firms. 11 firms were not directly comparable (as listed or VCTs) or did not have information available for some of their funds and are excluded from these calculations.

Not surprisingly, US firms in the sample had been in the VC business for longer, the earliest fund in the sample having been formed in 1981 compared to 1987 for the UK and 1994 for continental Europe. 14 of the US funds had been formed before 2000 compared to 4 in the UK and 5 in continental Europe.

When asked about their perceptions of the differences between the European and US VC environment 49% of firms commenting cited that the US has larger funds and/or that there is a lack of VC finance in Europe due to the smaller funds. 59% of UK VCs and 57% of continental European VCs commented on this compared to 32% of US VCs.

"There’s not enough top tier, early stage, series A-focused funds around (in Europe)’’: (US VC)

An Irish VC commented on the completely different situation in the US where there is a plentiful supply of VC finance, particularly in Silicon Valley:

“*I met a GP yesterday who is in a West Coast firm and, like, “I’m at Sand Hill Road. There’s more money, literally, on our road than there is anywhere else in the world for what we do.’’ And that kind of made me just stop for a second and, “Hang on a second here, I mean, we’re not even playing in the same division, we’re playing a different game.’’ It is a different world. So don’t try and repeat it. You’re doomed to keep making the same errors’’. (Irish VC)

Two UK VCs commented on the difficulties in raising new funds and spending too much time fund raising in Europe for the VC firms and on behalf of portfolio companies:

“The allocation of time between fund-raising and actually focusing on the investment business, is disproportionately the wrong way round’’ (UK VC).

“Everyone is worried here in Europe about just raising the next fund’’ (UK VC).

VCs need to have funds of a certain size in order to follow-on in subsequent funding rounds from their initial investment (UK VC 21). European VCs often don’t have the finance available in the proportionately smaller funds to be able to follow-on with the initial investments:
“In the US, if you start a company, you have an odds on chance of raising more money. In Europe, the single biggest risk of starting a new company is only one in five get further money, no matter how good you are.” (UK VC)

This can mean that they have to rely on syndication with other VCs, who they may or not know well, to a greater extent than in the US where, according to a US Silicon Valley VC, US funds have the ability to keep investing through all the rounds which means they can fund the company to a logical end point:

“I think a lot of European venture capital funds are loading up the ship but counting on the kindness of strangers in the middle of the ocean to get them to the next port and that problem means that even if you are going the right place and you had the right captain and the ship was doing well you’d still need the kindness of strangers to come in and help you refuel mid ocean and the problem with that is the stranger might extract most of the economics from you”. (US Silicon Valley VC)

Eleven of the non VC interviewees commented on the larger size of funds in the US, including 3 LPs, 2 entrepreneurs, 2 VC related, 2 advisors and 2 CVCs, consistent with the findings from the interviews with the VCs and with previous studies (Lerner et al, 2011). Twelve interviewees commented that Europe suffers due to its smaller funds; this results in difficulties in supporting follow-on rounds and in scaling (Coutu, 2014).

“There’s a massive inefficiency in the UK because you haven’t got scale of funds; you’re forever having to look to raise another round of funds and then another round of funds and at each break point for the next fundraising, there are valuation disputes, there are allocation disputes, it’s just hugely inefficient, a huge drain on management time”. (UK LP)

“Certainly, there’s lots of evidence to say we sell things earlier but I think that’s because we haven’t got enough money to build them into truly great companies”. (UK LP)

There was general agreement between the entrepreneurs interviewed that there are more funds in the US and more funds willing to follow up on an investment. The smaller size of funds and shortage of funds in the UK was specifically referred to by two of the entrepreneurs interviewed.

“You have many choices there (US) and very few choices here (UK) in terms of big funds that you want to follow up”. (UK Entrepreneur)

“We’ve got very big VCs on the US side and pretty small VCs on the UK side”. (UK Entrepreneur)

A European VC related interviewee commented that: “in Europe you just don’t find large enough VCs that could really bring you all the way up”.

Two LPs and one VC related interviewee did however mention that smaller funds can generate better returns than large funds. Gottshalg et al (2003) found that larger size funds do not necessarily perform better than smaller funds. There was general agreement about an optimal, mid-size fund level. Lerner et al (2011) proposed this optimal level as between $84m and $365M. One VC related interviewee in the US commented on the bifurcation of the US VC industry into 12 to 15 household name mega funds and an emerging group of micro VCs with fund sizes of less than $100m:
"The small focused funds have the potential ability to return the entire fund on a single investment. The large funds have the ammunition to build a company and support it till it becomes successful. The guys in the middle who have tried to do everything at all stages, who’ve struggled, who can’t put $100 million into a company, so can’t quite finance, you know, Facebook on their own and yet can’t get enough returns on a single company to return the entire fund, a no-man’s-land is this kind of $300 - $600 million funds. That’s the area where you’re really seeing the venture industry shrink". (US VC related)

Table 2: Size of fund, sector and stage stratification of VC firms in sample

<table>
<thead>
<tr>
<th>No. of firms</th>
<th>US</th>
<th>UK</th>
<th>Cont. Europe</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Size of fund</strong>*</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Small (&lt;$84m)</td>
<td>3 (12%)</td>
<td>9 (38%)</td>
<td>8 (53%)</td>
</tr>
<tr>
<td>Medium ($84m - $365m)</td>
<td>12 (48%)</td>
<td>13 (54%)</td>
<td>6 (40%)</td>
</tr>
<tr>
<td>Large (&gt; $365m)</td>
<td>10 (40%)</td>
<td>2 (8%)</td>
<td>1 (7%)</td>
</tr>
<tr>
<td><strong>Sector</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>IT</td>
<td>10 (40%)</td>
<td>8 (33½ %)</td>
<td>2 (13%)</td>
</tr>
<tr>
<td>Lifesciences</td>
<td>3 (12%)</td>
<td>2 (8%)</td>
<td>1 (7%)</td>
</tr>
<tr>
<td>Mixed</td>
<td>11 (44%)</td>
<td>8 (33½ %)</td>
<td>10 (67%)</td>
</tr>
<tr>
<td>Focused</td>
<td>1 (4%)</td>
<td>6 (25%)</td>
<td>2 (13%)</td>
</tr>
<tr>
<td><strong>Stage</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Seed / early</td>
<td>11 (44%)</td>
<td>11 (46%)</td>
<td>9 (60%)</td>
</tr>
<tr>
<td>Venture (incl early)</td>
<td>12 (48%)</td>
<td>13 (54%)</td>
<td>6 (40%)</td>
</tr>
<tr>
<td>Growth</td>
<td>2 (8%)</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

* as categorised by Lerner et al (2011)
Sector focus

As can be seen from Table 2, twenty VC firms in the sample invested in the broad technology sector (including such areas as internet, software, mobile communications, communications hardware, B2B and B2C e-commerce, consumer internet, mobile gaming, enterprise SaaS, enterprise IT, digital media, semi-conductors, internet web applications, multimedia, robotics and clean tech). Six VCs invested in lifesciences (including such areas as pharmaceutical and biotech products, medtech devices and diagnostics digital healthcare, therapeutic implant, pharmaceuticals, biopharma and drug delivery). 29 VCs invested in both tech and lifesciences and 9 VCs had a more focused approach to investing, concentrating on a particular segment within tech (such as SaaS, cloud, mobile, digital media, open source or internet). There was no particular differentiation between UK and US VC firms in their sectoral approach to investing. Continental European VCs had more of a mixed approach with 60% of the firms in the sample having investments in both technology and lifesciences. UK and continental European funds had more specialist focused funds proportionately than with the US VC firms, likely reflecting the approach adopted by some of the newer, smaller UK VC firms established in the last ten years.

Stage focus

There was a fairly broad distribution of VC firms in the sample across the different stages of investing and across UK, continental Europe and US. 31 VCs (48% of the sample) focused on seed and early stage investing, 31 VCs (48%) on venture (early to later stage). Only two VC firms in the sample, both US VCs, focused exclusively on investments at the growth stage (VCs 51 and 54). 60% of the continental European firms had a focus on seed and early stage investing, a greater proportion than with the UK and US firms. As noted above some of the more established UK VCs have been moving their focus more towards later stage investing. Lerner et al (2011) and Marston et al (2013) have concluded that the stage focus of funds, along with other fund characteristics, does not explain the magnitude of the difference in performance between UK and US funds.

Seed focus

As can be seen from Table 2, 48% of the VCs in the sample were investing at the seed and / or early stages (44% of US VCs, UK 46%, E US 60%). Some of the firms, particularly those based in Silicon Valley, invest at the seed stage on order to test the market as with two firms in the sample. One of these Silicon Valley based US VC makes seed investments from $50k to $1m to “test the water” particularly in the consumer sector:

“Let’s take a little of it and see if something pops. We’re not going to spend any time on it, we’re not going to go on the board, etc.” (US VC)

Another Silicon Valley VC has a $20m seed fund which it uses to make “experimental investments with far out things” which are not yet ready for full VC investment. This VC slims down the investment decision making process so that just one partner can decide on an investment of up to $250k in just one meeting with a company and four partners can decide on up to $500k in one meeting. Another VC in Silicon Valley has a sole focus on seed investments sometimes investing when there is no business plan.

A US LP commented on this “betting” on small seed investments:
“If you have a $200 million fund it’s very easy to make a series of small bets of seed stage, $250,000. That doesn’t hurt you very much and you get a lot of options on putting a lot of money to work behind the actual ones that work”.

Whilst this “testing of the market” is perhaps more common to the US Silicon Valley VCs there was one continental European VC who commented that they invest at the seed stage in order to get a “foot in the door”:

“If you don’t invest in a company, then you lose total contact with them. If you have a small investment, it forces you to do reporting to check regularly, etc and time flies very fast. So it is a very good discipline”.

Partner backgrounds

US firms in the sample had around one more partner in total than UK and continental European firms (US 6.4 per firm, UK 4.9, E 5.3). They also had proportionately more partners with particularly operational (US 2.7 per firm, UK 1.5, E 2.0) and, to a lesser extent, entrepreneurial backgrounds (US 1.0, UK 0.7, E 0.9). Lerner et al (2011) found a positive relationship between the number of partners and fund performance.

Table 3: Background of VC partners

<table>
<thead>
<tr>
<th>Whole firm</th>
<th>Financial/Investment</th>
<th>Consultant</th>
<th>Operational</th>
<th>Entrepreneur</th>
</tr>
</thead>
<tbody>
<tr>
<td>By no. of partners in sample:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>US</td>
<td>160 ptrs</td>
<td>39%</td>
<td>3%</td>
<td>42%</td>
</tr>
<tr>
<td>UK</td>
<td>117</td>
<td>48%</td>
<td>6%</td>
<td>32%</td>
</tr>
<tr>
<td>E</td>
<td>79</td>
<td>32%</td>
<td>14%</td>
<td>38%</td>
</tr>
<tr>
<td>By no. of firms:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>US (25)</td>
<td>6.4 ptrs/firm</td>
<td>2.5</td>
<td>0.2</td>
<td>2.7</td>
</tr>
<tr>
<td>UK (24)</td>
<td>4.9</td>
<td>2.4</td>
<td>0.3</td>
<td>1.5</td>
</tr>
<tr>
<td>E (15)</td>
<td>5.3</td>
<td>1.7</td>
<td>0.7</td>
<td>2.0</td>
</tr>
</tbody>
</table>

US VC firms have more partners with an operational and entrepreneurial background than with a financial / investment and consultant background (58 /42 split). UK firms have less partners with an operational and entrepreneurial background than with a financial / investment and consultant background (46 / 54 split). Continental European firms have more partners with an operational and entrepreneurial background than with financial / investment and consultant background (54 /46 split). Excluding one continental European firm with a particular focus on entrepreneurial partners (8 out of 12 partners) the remaining continental European firms have an equal number of partners with operational and entrepreneurial backgrounds and financial / investment and consultant backgrounds (50 / 50 split). Bottazzi et al. (2004) show that VC firms where the partners have previous business experience provide more support and governance to a venture. The greater concentration of operational partners in US VC funds may well contribute to improved performance, an area that has not been subject to much investigation in the past (Kelly, 2011).

Twelve of the non VC interviewees, including 2 LPs, 2 entrepreneurs, 2 VC related, 2 advisors, 2 others and 2 corporate VCs (US 7, UK 5) commented on the more operational and
or entrepreneurial experience of US VC investment executives compared to those in Europe, consistent with the findings from the VC interviews.

The operational / entrepreneurial background of investment executives is particularly evident in Silicon Valley, Andreessen Horowitz being given as an example of a VC firm that has “changed the game with their entrepreneurial background and operational approach” (US VC related).

“If you look at the genesis of the US West Coast industry they were people with genuine industry experience who knew what they were on about, knew the sectors they were working with and investing in and did very well out of that whereas, talking generalisations here, in the UK, our venture industries tended to be people who’d been at 3i and were trained as financial engineers. Too few were genuine scientists, technologists and business people getting involved in the early days. I think we had, in comparison to the US, a disproportionate number of people who were accountants and financial engineers who had been trained in the kind of development capital school of ICFC (3i)” (UK LP).

Europe is however catching up on this and many of the new VC firms established in the UK and continental Europe are run by former entrepreneurs. Entrepreneurial experience tends to be favoured over operational experience by LPs. The above UK LP went on to say that funds he is now backing are more like the early US West Coast firms:

“People who know and understand (cloud computing), probably better than anybody else. They have been there, seen it, done it, got the t-shirt in terms of running businesses” (UK LP).

Investing experience amongst VCs is however critical for LPs:

“Because of all the experience they have, quite frankly, they're just a lot more efficient and a lot more productive. And they can make more informed experienced judgments in terms of what's right, as opposed at somebody who's mid to late 30s. There's just no value for experience. And again it's investing experience, which is kind of the most important there” (US LP).

Two of the entrepreneurs interviewed confirmed the LPs’ comments on the difference in backgrounds between US and European VCs:

“US VCs are operational VCs, ex-entrepreneurs and have run companies whereas here in Europe they are more interested in all these financial details, financial alliances, maybe their background is as bankers or consultants. Which is not the case in the US; they are more hands on they understand, they are closer to the entrepreneur”. (UK Entrepreneur).

“People who are good entrepreneurs are often the folks who end up becoming venture capitalists here”. (US Entrepreneur)

Having both operational and / or entrepreneurial experience combined with financial skills is seen as an ideal ingredient for investment success:

“I think the venture capitalists who are successful have both a technical operational background as well as a financial acumen that is probably higher than your standard
individuals”. (US VC related).

Two of the advisors interviewed also commented on the difference in backgrounds with a focus on finance in Europe and on product in Silicon Valley:

“If I go to raise money from a European VC, I think a lot of it is about, “So how are you going to generate revenue? How are you going to get it to be profitable?”, Here the conversations tend to be more about, “What’s the product? What’s the market? How do you get the product to fit?” I think that’s a big difference”. (US Advisor)

The CVCs also commented that whilst most VCs have a finance background as opposed to operational background, “there’s a much higher percentage of people with operating backgrounds in VCs in the US than people with finance backgrounds”. (UK CVC)

The more operational / entrepreneurial background of US VCs certainly helps with marketing and origination / deal flow but data does not necessarily suggest that former entrepreneurs who invest get better performance:

“You might get slightly better deals because if you are an entrepreneur you might rather have someone who’s run a billion dollar company than someone who hasn’t” (UK VC)

“Entrepreneurs like to raise money from people who’ve done it already. I think you are much more comfortable if you’re running, starting a big data company, you might want to get the founder of X data management company on the board rather than someone who worked at an investment bank and then came up through the VC even if that VC is a really top VC”. (UK CVC)

Responsibility for deals

Whilst most VC firms have a lead partner responsible for deals from sourcing a deal through to exit, other partners are often involved at the due diligence or post-investment stages or indeed throughout the deal, sharing expertise on deals as and when required.

Table 4: Partners “own” deals

<table>
<thead>
<tr>
<th>Theme category</th>
<th>Themes</th>
</tr>
</thead>
</table>
| Partners “own” deals (US 20, UK 23, E 13)* | • 95% of all VCs had a lead partner responsible for deals from source to exit (three UK firms did not)  
• 85% of US VCs, 83% UK and 62% E VCs had other partners involved at due diligence or post-investment or throughout the deal  
• 40% of US VCs had two partners on deals cf 22% UK and 23% E |

*numbers in brackets under theme category on this and subsequent charts indicate the number of VC firms from each region who commented on the specific area.

Some firms have two partners assigned to a deal at all times. This may function effectively as a buddy” system. Having two partners involved can provide additional value add or the
second person may simply deputise for the lead partner as necessary. They may act as “devil’s advocate” or be someone who is an expert in the sectoral area or who is local geographically to the company. 40% of US VCs had two partners working on deals in this way compared with 22% UK and 23% continental European VCs.

Operational differences

The research investigated various aspects of the VC’s investment approach, including their investment strategy in terms of a higher risk, home-run approach as compared to a lower risk, growth approach, how they source deals, whether they invest in disruptive technology, how they carry out due diligence procedures and arrive at their investment decisions, the terms used in the deals, syndication, how they monitor portfolio companies once investments have been made, how they seek to add value to the investments and how they achieve exits. As explained below, the findings show that more US VCs pursued a home run investment strategy than European VCs, more US VCs do most of their due diligence in house, senior partners can force an investment decision in some US VCs and, more US VCs wait for the best exit and are proactive in achieving an exit than European VCs. A particularly interesting area, which does not appear to have been subject to academic investigation is the emphasis that US VC firms place on researching potential themes for investment.

Theme approach

The propensity and ability of VCs to predict future investment trends does not appear to have been subject to empirical research although Mason (2007) mentions that the sharing of information through VC networks can provide knowledge about likely technological trends to help VCs decide their investment focus.

All US VCs in the sample who were asked whether they researched future potential investment themes said that they used this approach (100%, 11 US VCs), going “deep” into a theme and looking for angles to differentiate:

“*I went out and met just about every start-up that I could that was involved in the (internet) real estate space and I think I probably ran through about 12 different projects*” (US VC).

Five UK VCs (71% of those who were asked or who commented on the theme approach) and three continental European VCs (75%) said that they used a theme approach although one of these UK VCs commented that they just “pretend to do it” as, in their view, do many other VCs:

“*There is more rhetoric than reality to it but we all do it; we all pretend we do it, yes. LPs like the idea. I’m being a little cynical about that.*” (UK VC)

Another UK VC said that they used to brainstorm for themes and that they “probably should do this again”.

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Table 5: Investment theme approach

<table>
<thead>
<tr>
<th>Theme category</th>
<th>Themes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Investment theme</td>
<td>All US VCs asked about theme approach said they used this approach. One UK VC said follow trend; one said pretend to do it.</td>
</tr>
</tbody>
</table>

Leading US VCs aim to spot investment trends early. A UK VC commented that:

“The majority of the quality venture firms actually know how to spot a trend, spot it early, and then find who are the companies worth backing; or who are the entrepreneurs in their stable worth backing into that trend”.

This VC went on to say that Europe doesn’t have “enough of that” and either the European VCs think that venture is about finding something “buried in a lab” or they look at trends that happened a year or two ago and try to continue the previous trend. A theme approach clearly takes resource, which as noted above and commented upon by a UK adviser (see below) is more available in US firms with their relatively larger funds and teams. Another US VC brings enormous resource to play in researching themes, resource that is simply not usually available to European VCs:

“Our 10 times per year partners decide where to put resource to try and identify an investment thesis, whatever it takes, and present to everyone in the group a thesis with respect to is there an investable idea behind that?” (US VC)

This firm carries out primary research, spanning out into their network of people, mapping out an entire industry and all the competitors therein. They find out what conferences they need to attend in the next 2 months and what companies they need to cold call.

A US Silicon Valley VC utilises what they term a “prepared mind” approach:

“We do those ‘prepared mind’ initiatives, so you try to develop a thesis around what you think is going to be a future area of investing” going on to comment: “that’s why venture investing is so hard because you don’t really know what you’re investing in”.

A UK VC referred to this “prepared mind” approach of US VCs whereby each partner specialises in one area and then has one or two associates working with them and “they’re really mopping up the area and really knowing it from A – Z. That’s hard to do unless you have a lot of resource”.

Whilst US VCs appear to adopt a rigorous approach to researching and developing investment themes European VCs perhaps pay it “lip service” as with one UK VC or do not profess to have the foresight to be able to predict future trends as with another UK VC who said that they follow the trend, focussing on sectors but as followers:

“That’s not done as a crystal ball like I’m cleverer than anybody else. But when there becomes more of a groundswell of investors who want to do stuff in that space because they tell me that they think it’s getting an interesting area, I follow them. I don’t profess to understand what’s going to be bigger”.

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Whilst not following behind to the extent of European VCs, US VCs may still be behind the entrepreneurs in which they seek to invest in their thinking as commented on by a US East Coast VC:

“The problem with a thesis approach is that it’s the entrepreneurs who find the “wide spaces” and tell you where the markets going. Whenever VCs try to define trends, they tend to be slightly looking back, slightly boring, and slightly undifferentiated” (US East Coast VC).

It is by talking with entrepreneurs and other “movers and shakers” through the VCs’ extensive networks that enables VCs to spot emerging trends:

“We tend to be people investors. We think that the entrepreneurs are the smartest folks and that the object is to get them to tell us about what they’re working on and so we go out of our way to find the opportunities for them to explain what they’re working on and hope that we have the foresight to say, “Ha! That’s interesting, we should do it.” (US West Coast VC).

Two US VCs specifically commented that they do not follow the herd, they do not chase “fads”. One of these VCs said that they keep close contact with lots of potential customers, they talk with CEOs, organise events, understand what needs are not being met by existing products, read Gartner, IDC, 451 Group (emerging tech) reports and derive a theme:

“Typically we find that coming up with a thesis and canvassing that landscape and putting together real analysis behind it before reaching out to the companies and investing, tends to create a better framework for investing than sort of waiting to see what comes to us or opportunistically investing in different opportunities”. (US VC)

A US mid-Atlantic VC looks for discontinuities in an industry:

“We do a thing called a discontinuity round table: we talk, we get a topic, we do a bunch of research on it, we think it’s an interesting area and then we pull a group of people that are really world class kind of folks, discuss for two days about that topic and really hone down to a specific strategy we want to go after”.

A continental European VC commented that they don’t have the means in terms of resources to do a lot of research into areas to invest in but they do collect signals from firms investing at the seed stage and from incubators and accelerators: “not really to do the deals but more to be aware of what’s coming up on us in the Series A stages”.

Other VCs were silent on a theme approach or the lack of it, generally investing in sectors in which they had existing expertise or could gain access to expertise.

The wide adoption of a theme approach was confirmed by the non VCs. A US LP commented on how US VCs “network like crazy” using their extensive networks to establish themes. The US VCs that he deals with (based on the East coast) do not carry out market research or use consulting firms such as McKinsey to establish themes:

“They are just sort of are out there talking to a lot of people, synthesise a lot of information, hear a lot of good ideas and a lot of bad ideas and over time I think they’ve just developed
judgment”. The well-known VCs in his geographic area for example “just understood social networking earlier than anybody else did and they made a series of interesting bets and they’ve played out incredibly well”.

A former senior player in the industry commented on how the top VCs in Silicon Valley are “ahead of the curve” in understanding technology and being able to get technology into beta sites when the companies were loss making and just had proof of concept.

A UK advisor commented on UK VCs indeed having fewer resources to spare on theme research and with US VCs having more of a “top-down” approach to investing compared to more of a follower approach in Europe:

“That’s traditional of US VCs. Something in Europe people don’t do nearly as much. I think partly because they have smaller funds and therefore they have fewer resources to spare on this kind of exercise. So I think it’s a question of resources, probably goes back to the question of your level of energy and aggression and I guess commercial acumen. In Europe it tends to be I think more let’s try to pick an angle we think is less; you know perhaps less traded on than some others”

A UK based partner of a large US corporate VC commented that they even employ their own futurologists and leverage all the knowledge they have about markets in order to come up with investment themes.

Whilst a number of UK VCs do say that they follow a theme-based approach to investment trends it is clear from the above comments that they do not do this to the same extent of the US VCs. This is partly due to a lack of resources to carry out the necessary research and partly due to the less use of, and less availability of, networks of entrepreneurs, technologists, large technology corporates and other stakeholders to share information on new technology trends. Hochberg and Ljungquist, (2005) found that the better-networked VC firms achieved significantly better fund performance. Networks and the sharing culture are discussed further in the section on cultural differences.

BVCA Committee members agreed that US VC firms carry out more research into the next “hot” areas for investment. They do this largely in-house and by using their extensive networks; not by engaging outside consultants. They excel at capturing information and developing knowledge-banks:

“It’s about proprietary research and proprietary analysis, that’s what these guys do. They leverage their network. So, they actually have smart people like McKinsey but they don’t need to… no-one hires McKinsey in the VC business because you can get so much closer to the edge by talking to the entrepreneurs, talking to other VCs, making some mistakes and actually hiring really bright people and putting them to work. They hover around Techstars and they hover around conferences and they read every blog that’s out there and they go and meet as many companies as they can”. (UK CVC*)
Focus on disruption

VC firms from all regions like to invest in disruption as this provides competitive advantage for portfolio companies potentially leading to excellent returns for the investors. Disruption could be either in terms of the technology or product being disruptive (the principal approach to disruption), or the business model or the market. The term “disruption” was coined by Prof Clayton Christensen of Harvard Business School and means a new technology that unexpectedly displaces an established technology. For those VCs asked about whether they insisted on investing in disruption, most cited technology (2/3 US VCs, ½ UK and all but one continental European VC), though a third of UK VCs cited business model and a fifth cited markets.

Table 6: Disruptive

<table>
<thead>
<tr>
<th>Theme category</th>
<th>Themes</th>
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<tbody>
<tr>
<td>Disruptive (US 9, UK 19, E 8)</td>
<td>• Technology (US 6, UK 9, E 7)</td>
</tr>
<tr>
<td></td>
<td>• Business model (US 2, UK 6, E 2)</td>
</tr>
<tr>
<td></td>
<td>• Markets (US 1, UK 4, E 0)</td>
</tr>
<tr>
<td></td>
<td>• Not necessary (US 1, UK 4, E 1)</td>
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Investment strategy

VCs tend to pursue either a home run, “1 in10” investment strategy when they select deals for investment on the high-risk basis that at least one out of every ten investments they make will return the fund as a whole (Zider, 1998) or they pursue the less risky, and potentially lower return basis of achieving a 2x to 5x return on all their investments (growth strategy). This usually depends on whether they are investing at early stage or later stage. VCs can choose as to whether to invest in a high risk proposal or not. A higher risk strategy, such as the “1 in 10” approach can lead to higher returns by the performance of outlier investments that can return the fund as a whole.

In the sample of VC firms interviewed it was apparent that more US VCs pursued a “1 in 10” investment strategy (87%) than UK (60%) and continental European VCs (57%), potentially leading to outlier returns:

“So you have to be absolutely willing and ready to lose companies and to push them really hard on going big. The battle is being won by people who produce big exits”. (US VC)

“The top decile funds (in the US) would have a 40% failure rate and it’s called the Babe Ruth effect. So, it’s ‘I swing big, I miss big, but I hit big.’ So, it’s like you just go for it”. (UK VC)

The greater proportion of US VCs in the sample embracing a “1 in 10” strategy was not due to there being more early stage than later stage investors in the US sample as the proportion of purely early stage VCs in the US sample was 40% compared to 45% in the UK sample and 57% in the continental European sample.

More recently established UK VCs in the sample, ie those formed since 2005, pursued a “1 in 10” strategy, although one of these said that they do not necessarily pursue home runs. One of these newer VCs adopts an even riskier “1 in 20” model. Another commented that:
“You need some real outliers to drive returns. Our model is to try and find a couple of deals in the fund that are fund returners” (UK VC).

Two VCs in the UK with US connections also adopt the higher risk strategy of US VCs. They commented that their LPs expect them to take risks:

“When we speak with one of our LPs in particular I mean their constant push is “are you taking enough risk in your portfolio?” (UK VC).

A newer UK VC commented on the expectation of its LPs: “a lot of the thinking about the strategy has evolved through input from our LPs, particularly the US guys who are very focused on this hits driven model for venture capital funds”.

There was a perception that European LPs place more constraints on investment by European funds than do US LPs in US funds. They exercise more restraint about the risk approach of VCs and where funds place their cash, in terms of stages, sectors and specific countries.

“Certain LPs are quite limiting in their desires and constraints they place on the money. Having 40% European money also skews things because it means it’s investing on a different basis than the US LPs are investing” (UK VC).

A continental European VC that adopts the “1 in 10” model “like the US style” stated that its approach differs from others in Europe who go for smaller exit perspectives, smaller investments and a lower downside risk.

Table 7: Investment strategy

<table>
<thead>
<tr>
<th>Theme category</th>
<th>Themes</th>
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<tbody>
<tr>
<td>Strategy (1 in 10 approach) (US 16, UK 21, E 14)</td>
<td>• 87% of US VCs pursued a 1 in 10 investment strategy or at least a 10x expectation of 60% UK and 57% E VCs</td>
</tr>
<tr>
<td></td>
<td>• 43% of E VCs, 38% of UK VCs and just 13% of US VCs stated that they specifically did not pursue this strategy</td>
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Of course a “1 in 10” strategy doesn’t suit the risk profile of all early stage VCs, even US ones:

“Anybody who can tell you they swing for the fences on every single deal that they do and that’s what they go for doesn’t have a snowball’s chance in hell of building a real successful portfolio because you just don’t know” (US VC).

The adoption of more of a “1 in 10” investment strategy by US VCs is a reflection of the intense competition in the US VC environment, particularly in Silicon Valley:

“It’s unbelievably competitive (in the US). You’ve already got four or five competitors in the way that you don’t here (in the UK) so you kind of have to win, the middle ground doesn’t work” (UK VC).
Consistent with the finding that more US VCs stated that they pursued a “1 in 10” investment strategy than European VCs, in this present study 5 non-VCs who commented on investment strategy confirmed the more risk taking approach, particularly of Silicon Valley based VCs (2 VC related, 2 advisors and 1 CVC). The two advisors commented as follows:

“You see more deals that look crazy out here by people who made crazy bets and they come off because no one really knows what's going to happen in the next two years. It’s the Wayne Gretzky “play to where the puck is going to be, not where it is” and I think the best venture capitalists here are very good at doing that but they place big bets and not all of them come off” (US advisor).

VC related interviewees also commented on the more risk taking approach of US VCs, particularly in Silicon Valley:

“The risk taking culture here (in Silicon Valley) is of the notion of swinging for really big outcomes, outsize outcomes. When you move to Boston, the UK or the East Coast in general (and New York is a slightly separate little bubble that is developing) talking about the traditional Boston market it was a little more conservative meaning that there’s more thought to risk litigation, checking your downside a little bit more, accepting outcomes that were good but not ginormous” (US Silicon Valley VC related)

A UK advisor confirmed that the newer, smaller VC firms in the UK are pursuing more of a risk taking “1 in 10” approach.

**Deal sourcing**

VC firms may source deals in several different ways. Some proactively go out into the marketplace and find suitable companies in which to invest. This approach requires an in-depth knowledge of the particular sectors in which the VC firm operates. Other firms might rely on their brand name, profile in the marketplace and track record in working with successful portfolio companies to attract deals; more of a reactive approach. Deals may come via the proprietary networks of the executives in the firms. In the sample of VCs interviewed in this study, more UK and continental European VCs cited a proactive approach to sourcing deals than did US VCs (UK 43%, E 50%, US 26%). More US VCs cited their brand name, profile in the marketplace and track record as the principal means whereby deals are sourced (US 26%, UK 9%, E 8%). This may be associated with the extremely competitive environment in which they operate, particularly in Silicon Valley. This is where having a well-established brand name to attract the best deals certainly helps:

“I certainly think a company like Facebook has had wide-ranging global impact on the brand” (US Silicon Valley VC).

64% of all US VCs who commented on competition mentioned the (very) competitive environment in which they operate. The highly competitive environment in Silicon Valley was acknowledged by all of the US VCs who were interviewed from this area and by a UK VC and a continental European VC operating in Silicon Valley. Competition was less intense for VCs from other US regions and for those with a lifesciences focus. 78% of UK VCs and 40% of continental European VCs said that there was very little competition, although two continental European VCs mentioned the competitive nature of later stage deals.

Due to the highly competitive market in US there is the need to differentiate in some way:
“You definitely do need to differentiate if there’s a new fund in the US. I think that’s the competitive thing. There’s a new fund; you can’t just add money, you’ve got to have something else that you’re bringing to the table” (UK CVC*)

The new funds in the US are also trying to pitch against an unbelievably sophisticated market that already exists which is not the issue in the UK, according to a UK VC*.

Table 8: Deal sourcing

<table>
<thead>
<tr>
<th>Theme category</th>
<th>Themes</th>
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</table>
| Deal sourcing (US 23, UK 23, E 12) | • More UK and E VCs cited a proactive approach to sourcing deals than US VCs (UK 43%, E 50%, US 26%)  
• More US VCs cited their brand name/profile/track record as key for attracting good deals (26% cf 9% UK, 8% E)  
• Personal networks/proprietary deals were more important to UK (52%) and E VCs (33%) than US VCs (26%)  
• More US VCs referred to deals being highly competitive |

Seven of the non VC interviewees (including 4 LPs, 2 VC related and 1 CVC) commented on the strength of the brands of US VC firms, particularly those in Silicon Valley, which aids quality deal flow and optimal exits often through relationships with big corporates. There was general agreement between the LPs that big brand name firms, as are seen in the technology hot spots of the US, obtain the best deal flow, entrepreneurs with exciting technology seek them out, have better access to strategic partners, customers and investment bankers and the best LPs invest in their funds. One of the US LPs cited this as one of the reasons for the difference in performance between US and European VCs and two LPs (UK 1, US 1) specifically mentioned the high brand strength of US VCs vis a vis European VCs.

“I can't think of European VC backed firms that would have the same kind of brand franchise for a start up that would be as attractive as some of the Silicon Valley groups here in North America”. (US LP)

“They just have to tell the world that Kleiner Perkins has invested, so the self-fulfilling, success has a self-fulfilling effect also, which the Europeans are bereft of”. (UK LP).

There was general agreement from the VC related interviewees about the success of brand name firms in Silicon Valley:

“I think there’s an element of ‘success begets success’ because you start building a brand and that starts pulling in the best entrepreneurs to the best funds. Sequoia is absolutely there”. (US VC related)

Personal networks and proprietary contacts were more important to UK and continental European VC firms (UK 52%, E 33%, US 26%). European VCs are more concerned to keep
proprietary information to themselves for competitive advantage in contrast to more of a willingness by US VCs, particularly on the West Coast, to share information.

**Due diligence**

VC firms may carry out much of the due diligence on potential investments in-house; they will form their own views as to the strengths of the management team, the attractiveness and growth potential of the market and the uniqueness and reliability of the product. Others may also involve external experts to a greater or lesser extent. In the sample tested more US VCs performed much of their due diligence in house; UK and, particularly continental European VCs were more likely to use external experts for technology, financial, IP and legal due diligence (US: 76% in-house cf UK 52%, E 60%).

Table 9: Due diligence

<table>
<thead>
<tr>
<th>Theme category</th>
<th>Themes</th>
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</thead>
<tbody>
<tr>
<td>Due Diligence (US 25, UK 23, E 15)</td>
<td>75% of US VCs do DD largely in-house cf 52% UK and 60% E VCs</td>
</tr>
<tr>
<td></td>
<td>Only 20% of US VCs use external experts for tech DD cf 43% UK and 67% E</td>
</tr>
<tr>
<td></td>
<td>Only 12% of US VCs use independent accountants for financial DD cf 35% UK and 47% E</td>
</tr>
<tr>
<td></td>
<td>Only 12% of US VCs have external advice on IP cf 26% UK and 33% E</td>
</tr>
<tr>
<td></td>
<td>Only 12% of US VCs have external legal advice cf 39% UK and 47% E</td>
</tr>
<tr>
<td></td>
<td>48% of US VCs did not mention tech DD cf 26% UK and 20% E</td>
</tr>
</tbody>
</table>

The use of external due diligence experts may depend on the specific company and opportunity. If outside the core area of a VC firm’s in-house technology expertise external consultants may be engaged. In the case of market due diligence many VCs do primary calls on the market themselves. They may interview industry experts and/or call investment bankers who cover certain industries.

“We do a lot (of due diligence) in house but no matter how good your own team is technically you can never really understand every product to the fullest extent so we always bring in know-how from our board of advisors...or the networks of those guys”: German VC; contrasted with the following comment from a US VC:

“We only invest in areas where we have the expertise in house. If we can’t diligence it because it’s not an area we know and understand we are not going to be helpful to the company”.

**Investment decisions**

95% of VC firms in the sample had an investment committee at which potential deals are discussed and eventually approved if due diligence and other enquiries are successful. In general the investment committees were comprised of those partners responsible for making investments. In some VC firms partners with an operational role for the firm and/or the CFO may also sit on the investment committee.

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Table 10: Investment approval

<table>
<thead>
<tr>
<th>Theme category</th>
<th>Themes</th>
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</thead>
<tbody>
<tr>
<td>Investment committee (US 22, UK 24, E 15)</td>
<td>• 95% of VCs had an investment committee (three US VCs were informal)</td>
</tr>
<tr>
<td>Investment decision (US20 UK 20, E 11)</td>
<td>• More UK and E VCs reached decision unanimously than by consensus; US VCs were equal here</td>
</tr>
<tr>
<td></td>
<td>• In four cases with US VCs (20%) a senior partner could force a decision</td>
</tr>
</tbody>
</table>

Whilst the partners may comprise the formal committee others can get informally involved. In a UK VC included in the sample the formal investment committee is just the partners but in practice everybody sits round the table and has an equal part in the discussions.

More UK and continental European VCs reached investment decisions unanimously than by consensus. Often the objective is to reach agreement rather than just vote:

“We would if it came to it have a majority vote but in reality if someone is really uncomfortable we’d like to find out why and we wouldn’t go ahead if someone was violently against something”: UK VC.

Whilst most US VCs reach investment decisions equally unanimously or by consensus, a senior partner could force a decision at 4 of the US VCs:

“What we found was that consensus would kill the outliers. Anybody who feels strongly about something can make it happen”: US VC.

This approach can mean that US VCs are more likely to decide to back very high risk propositions which can potentially lead to outstanding returns.

Two of the LPs interviewed mentioned that they prefer the core team, who have the largest share of the carried interest in a fund, or indeed a senior “rainmaker” to have the decision rights:

“When you get back to the successful firms it’s been our experience the more concentrated the GP decision making, obviously it has to be a good person, an experienced person that you’re concentrating on, but if you find that special person and then they have kind of concentrated authority or responsibility in the firm then your odds of success go way up”. (US LP).

In fact, one US LP said that they will only invest in VC firms where the decision making for investments (and exits) is concentrated with the founding partners who have experience and “scar tissue”. 

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Investment terms

In the sample, more US VCs had “entrepreneurially friendly” terms in their term sheets than UK and continental European VCs (US 57%, UK 23%, E 14%). US West Coast VCs are more entrepreneurially friendly than East Coast VCs. “Entrepreneurial friendly” terms means that the valuations offered by the VCs are more attractive to entrepreneurs, often due to the competition involved in doing deals as noted above which is particularly evident in Silicon Valley, and more onerous terms are not included. In contrast “investor friendly” terms may include full ratchets, multiple liquidation preferences and cumulative dividend streams. 42% of US VCs cited the use of entrepreneurially friendly terms as a key difference between US and European VCs, compared with 32% of UK VCs and 36% of continental European VCs.

“If you look at a venture deal structure, it’s probably the most lenient here and it gets kind of more onerous as you go east”: US Silicon Valley VC.

“‘We tend to have more of a west coast model. The east coast, they’re more financially driven, so they have more punitive terms. My experience with European venture capitalists is very similar... a lot of similarities to east coast investors in the US’: US Mid-Atlantic VC.

Table 11: Investment terms

<table>
<thead>
<tr>
<th>Theme category</th>
<th>Themes</th>
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| Investment terms (US 21, UK 22, E 14) | - 57% US VCs used entrepreneurial friendly terms cf 23% UK and 14% E VCs  
- 23% UK VCs had used ratchets cf 14% US and 14% E VCs  
- 71% E VCs referred to liquidation prefs cf 36% UK and 29% US VCs  
- Only UK and E VCs referred to dividend requirements |

“This is a cultural thing, in California we ask the question, well if everything this guy says is true, how big can the outcome be? In Europe they ask the question, what are all the ways this guy could be lying to me?: US Silicon Valley VC.

In this VC’s view European VCs are looking at every reason to say “No”:

“Europeans are saying how do I not lose and Americans look at the question how do I win?”

This illustrates the long-held views on the cultural differences between the US and Europe in terms of ambition and propensity for risk which have been acknowledged as possible contributors to a performance gap (Lerner et al., 2011), see section on cultural differences.

UK VCs in the sample tend to use ratchets more and continental European VCs use liquidation preferences more than US VCs. Only UK and continental European VCs referred to the requirement for dividend streams.

“No American CEO wants a European VC. I worked for a European VC because they do things exactly as you describe. What are our dividends that we’re going to get? Questions that American VCs just vomit all over”: US Silicon Valley VC.
In contrast Kaplan et al. (2004) found less use of convertible securities and contingent control provisions in VC contracts with a predominant European component.

Nine of the non VC interviewees agreed with this concept of the difference between entrepreneurially friendly and investor friendly terms. Of these six were commenting on the difference between US and Europe, with the US being seen to be entrepreneurially friendly and Europe being seen to be investor friendly (2 VC related, 1 advisor, 3 CVCs) and three agreed with the difference between East Coast and West Coast VCs (1 entrepreneur, 2 CVCs).

A US CVC commented as follows on the East versus West Coast approach:

“East Coast is more about Wall Street type marking your valuation up as high as you can, as quickly as you can, versus the West Coast approach which looks at the longer term a bit more and can see the down side of marking up a valuation too high, too quickly”. (US CVC)

The use of more entrepreneurially friendly terms by US VCs could be stage related with more onerous terms used at the later stages:

“I think there is a lot of holding the feet to the fire in the US funds, much more so than here, particularly in the mid to late stage valuations where the valuations are very, very high. Often there are some pretty onerous terms in their preference and the like that if they don’t hit their numbers then they start kicking in. So, it’s not all as value friendly at the later stages as it might seem”. (UK CVC*)

Europe is perhaps more cautious because of historic poor performance:

“The history and the track record of the industry in Europe is things go wrong most of the time and when it goes right it doesn’t go very far. It’s actually quite rational to think maybe I should be a bit careful here”. (UK advisor),

and so the use of more investor friendly terms is entirely rational and problems with scaling makes it reasonable for UK VCs to want to protect the downside:

“There is such a track record of failure of European and Israeli companies trying to break into the US. It’s much harder than people think and it costs a lot more money. Then it becomes entirely rational to want to protect a little bit more of the downside when the upside does require another jump. Whereas, in the US you can scale. In the US you can achieve your billion dollar plus exit completely from the domestic market with a few bits of slides and a couple of guys on the ground in Europe. And that, I think, even in the world of the internet that’s true. There are only a few companies in Europe that can buck that trend. (UK CVC*)

Some VCs mentioned that the general approach to investing in the US, including the use of standardised documentation for early-stage deals, is much more consistent amongst firms than in the UK. This is exemplified by a more uniform cadre of limited partner investors in the US having a similar approach to risk:

“The US market is a lot more consistent. It’s a lot bigger; it’s been around a lot longer. People talk about what they do and their funding sources are all fairly similar so it’s either LPs or rich people. In Europe you’ve got lots of funny different pockets of money be it EIS, individuals, government funds, VCs who are small bits of private equity firms through to UK
arms of US VCs. And they’ve all got different risk profiles and approach. (UK VC*)

Milestones

Milestones are used to set goals that a management team has to reach before additional financing tranches are put into a company by a venture capital firm or management salaries are reviewed or share options granted. The term sheet may specify different milestones with regard to technical, production, marketing or financial progress.

Milestones were mentioned as being used by only a small number of the firms interviewed, just 16% of US firms (4), 21% of UK firms (5) and 13% of continental European firms (2). One US Boston-based VC said

“We don’t use milestone finance. To me that’s a fool’s errand because as we know and, this is a cliché, your business plan is invalid the moment you hit the send button”.

A US Silicon Valley VC agreed with that view:

“Drip feeding money in provided the company reaches milestones is detrimental”. This is because if the milestones are too onerous, or too geared to incentivisation, management may focus all their efforts on meeting the milestones to the detriment of the overall business

But milestone financing can help mitigate the risk of an investment. An Irish VC tranches financing based on milestones over the following 12 months at the micro level or over 3 years at the macro strategic level. If agreed milestones are not achieved then the VC does not invest at the pre agreed price. The VC prefers this approach than an alternative approach of lowering risk in terms of the pricing of the transaction.

A UK VC often tranches investment with half the money paid upfront and half later on at pre-agreed terms based on milestones; this is renegotiated if the company is off plan.

Another UK VC uses milestones and tranche payments due to the early stage nature of tech companies and the associated higher risk.

Some US VCs would just see this as undercapitalising companies, eg: a Silicon Valley VC said that:

“American CEOs think that European VCs just want to drip-feed them; the European VCs under-capitalise companies”.

A view confirmed by a US adviser:

“The European VCs, and I’ve dealt with French ones and UK ones, tend to be a lot more conservative. “Let’s give it as little as possible and see how far we get”. It’s kind of a dripping model versus a fire hose model”. (US Advisor)

Whilst there may anecdotally be more drip-feeding of finance into European companies by VCs, milestones are not uncommon in the US:

“I think there’s a lot of milestone investing in the US, actually. I think, again, another level down from that, they do put more money in but then they expect more and they drive to the
outcome they expected and then they don’t fund anymore, they maybe just reshape it, they may help the company merge, they will use their networks in all kinds of ways but there’s very clear milestones”. (UK CVC*)

Whilst milestone financing did not appear to be used to a great extent by the US technology focussed VCs in the sample it was used by US VCs in the sample that invest in lifesciences companies. A US Pittsburgh based VC used the milestone approach with its medtech investments with three different tranches of finance being provided: the first money to build a working prototype, then a second round, then a third round when the company had applied for FDA approval.

A US East and West coast based lifesciences VC looks at putting $20-25m to work in total but in tranches based on milestones. The initial amount provided can be small, eg for a de-risking event (ie. something that would otherwise kill a deal if a larger amount were to be invested). A US East coast based VC investing in both lifesciences and technology prefers to put all its investment in on day one rather than drip feeding at the initial round but does use milestones when it comes to subsequent rounds:

“Nothing is ever black and white really so you always have to make a judgment call when you get to that moment for the milestone”.

A further East coast based VC said that milestones may also be used if company gets into difficulties later on or if a syndicate becomes “unruly”, in the sense that “some want to play and some don’t”.

So whilst milestone financing appears relatively infrequently used in the sample of VCs interviewed it is a technique that can be used by VCs in the US, UK and continental Europe to help minimise their risk exposure.

**Syndication**

Many of the VCs in the sample syndicated with other VCs on their investments, usually locally but sometimes internationally. Anecdotally it is claimed that there is perhaps more of a tendency to syndicate for monetary reasons in Europe compared to the US, as previously reported by Manigart et al (2002). Syndicating for monetary reasons may be due to the relative scarcity of funding in Europe for scaling up ventures:

“We will raise more money to scale production. It’s a very liberating investor to have, saying if you had more capital could you be more ambitious with this? Having X as an investor added value because it gave the company more options”. (UK VC).

In the US syndication is often for non-monetary reasons:

“It’s better to syndicate, better to have other people around you to help you but I think you do that from a position of strength. We syndicate not because we need to (we have the ability to write the whole cheque if we wanted to) but because we want to”. (US VC)

Three of the non-VC interviewees commented on the need for additional financial resources as a reason for syndicating in Europe (1 LP, 1 advisor, 1 CVC).
Some US VCs do also appreciate the additional finance and reduction in risk that syndication provides:

“We want someone whom we think is rational who we have a personal relationship with who also has a deep pocket as part of our syndicate and so doing things on your own doesn’t make any sense because you don’t know what bad things will happen”.

(UK VC).

Many VCs commented on the importance of relationships to successful syndication.

“We’ve had lots of bad experiences (with syndication). So, you’ve got issues of funds of different vintage, you’ve got different mindsets, people may be not as commercial, or just have a different view of life. Disagreements over what should be done with companies, whether there should be more money, or whether there should be a change of management team. We’ve had lots of suboptimal experiences”.

(UK VC).

The concentration of VC firms in Silicon Valley facilitates the syndication of investments by VC firms (Zhang, 2007). There was general agreement between VC related interviewees that large US VCs syndicate to pool expertise even though they can fund the whole investment

Syndicating for monetary reasons can have a negative effect for some syndicate members:

“Because it’s the last man standing with money in his pocket that gets the best terms and the best return from the investment”.

(UK LP)

In the US VCs might syndicate to weed out the best companies and to get an early foot in the door to exciting new technologies, for example on the West Coast VCs might say:

”Actually, we’re all pretty impressed with search engine technology so we’ll all invest in a dozen search engine companies and then we’ll kill the ones that aren’t performing and we’ll all carry on syndicating in the ones that do perform”.

(UK LP)

Six interviewees (1 LP, 1 VC related, 2 advisors, 2 CVCs) referred to the difference in risk approach and /or style between US and European VCs and the impact on their willingness to syndicate:

“I had this recently with a couple of French VCs, all feared the US VCs. They didn’t want US VCs to get involved because their appetite for risk is much higher and they’re much more willing to throw a lot more at a problem or at an opportunity”.

(US advisor)

Hege et al (2009) reported that US firms do worse investing in Europe and Europeans do better investing in US. This may be due to this difference in approach.

“Europeans with US syndicates will get a lift and the US with European syndicates will get a drag. Europeans go over there and they co-invest alongside Accel or NEA, they will suddenly find, we’re getting a brilliant ride here. Can’t believe those guys just went to the board meeting and told the Chief Executive that he’s not to go into the Indian market or Chinese market. You know we would never tell people, we’d discuss it with them”.

(UK LP)

VCs tend to be very “cliquey” in Europe according to a UK advisor in terms of the firms with which they syndicate and a proprietary approach to investing. This was confirmed by a US VC related interviewee:
“When I got to the UK in the early days there was a combination of two things: one is a sort of more “I want this deal to myself” you know what I mean? And number two was it’s a small universe of VCs and so it’s not as natural to find a partner where it’s hard to go from a situation where you are really banging heads and competing hard on a deal and in the next breath saying “well why don’t we work on it together” right, I mean in the US there are enough firms where the co-opetition can just exist more naturally”. (US VC related)

Whilst there was no particular evidence of less syndication activity in Europe compared to the US in the VC firms sampled in this study, Schwienbacher (2005) found that syndication is used more often in the US. One UK LP said that US has more syndicated deals because there’s a wider base of VC managers from which to invest:

“Whereas in Europe now there’s so few managers around and European managers have sometimes had bad experiences of being in larger syndicates so I think they’re less likely to syndicate than their US counterparts”.

In the US because it’s a cradle to success approach there’s a kind of “lingua franca” of what it means to execute a successful playbook amongst syndicate members. In the view of one UK CVC this “lingua franca” is not evident in the UK:

“You can’t emphasise enough how much friction there is because you know you’re not just educating a company you’re educating the investor group. Therefore, when the offer comes in to fund it may be out of synch with what the investors want”. (UK CVC*)

Monitoring and portfolio reviews

95% of UK VCs took a board seat in the sample of VC firms interviewed, compared to 73% in the US and 67% in continental Europe. In contrast to Schwienbacher (2005) there was no evidence that European VCs spend less time monitoring their investments than US VCs:

“In our rule book anyway; you should be spending a day a week with the company if you’re doing your job properly”. (UK VC)

Table 12: Monitoring

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<th>Theme category</th>
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| Monitoring (US 22, UK 20, E 12) | • 95% of UK VCs take board seat cf 73% US VCs and 67% E VCs  
• 30% UK VCs take observer role cf 27% US VCs and 8% E VCs  
• Four UK VCs said they limit no. of board seats cf one US VC (one US VC said no limit)  
• Weekly contact with portfolio companies was most popular in all three regions |

VCs review their portfolio companies often quarterly for the purpose of reporting to their LPs. Reviews are also carried out for considering whether to follow on with subsequent rounds of financing and for the level of support that is provided to portfolio companies. This might involve a formal rating of investments every 6-8 months as reported by one UK VC or an informal rolling review, two to three times per year as reported by an Irish VC. Some VCs
review all their portfolio companies each week, not just new opportunities, as reported by an East Coast US VC. One of the purposes of such reviews is to identify and cut off losers as early as possible and to concentrate on supporting the better performing companies in the portfolio.

“Here’s ten companies, arrange them one through ten in terms of the ones you think are going to make it,” you usually tend to agree on the top three or four and you usually tend to agree on the bottom three or four, alright? So the discussion is really about the two or three in the middle … but normally, everyone normally can spot the ones that aren’t going to make it”. (UK VC)

Though there was no particular difference in the approach of the US and European VC firms in the research sample as regards portfolio reviews, BVCA Committee members commented on the focus on monitoring investments with formal portfolio reviews and weeding out of underperforming investments by US VCs. This is partly due to the higher risk approach to investing by US VCs.

“There is one very successful (US early stage) fund that we’ve worked with a couple of times. They tell the companies on the way in ‘you will be triaged and we have three layers of triage; there is the continues to fund, the wait this one out, and the we won’t invest in you again’ And they mine the data and they are very, very clear about not continuing to invest and the amount of money. They’ve got very strong US returns as a result of that.

Clearly, if you’re expecting a 40% failure rate you are going to be very, very closely focused on is this the one where I pull it all” (UK VC*).

Four UK interviewees, including 3 LPs and one advisor, commented that European VCs tend to keep poor investments going for longer whereas US VCs would cut their losses.

“Europe is learning from this and I think that’s one of the mistakes that’s past, I think they are learning to call things more quickly. Again maybe it comes back to the fact that the US have much larger portfolios so it is easier emotionally to let things go when you’ve got a bigger portfolio than when you’re in a smaller portfolio. (UK LP)

As indicated in the above comment this tendency to keep poor investments going may be due to the smaller fund sizes in Europe as mentioned by another UK LP:

“They (US VCs) can afford to because the proportion of their fund size – so we’re talking about the successful investors here, the big ones – that they’re putting into each investment at an early stage is relatively small, so they can afford to walk away from them without impacting the total fund performance. In the UK, with smaller funds, the proportion of the fund of each investment is going to be larger and, therefore, there’s going to be greater reluctance to walk away and admit you got it wrong”. (UK LP).

It also may be due to a lack of courage and self-confidence on the part of European VCs:

“Leading (US) VCs, like Sequoia and KP, have the courage to cut. I think the difference between those that are great venture capitalists versus those that are not is to have the courage to do that. In Europe we keep things going for too long because we’re lacking self-
confidence and therefore admitting defeat is difficult and obviously our paltry track record is disastrous”.

(UK advisor)

Interestingly, in contrast to the above comments from the non VCs, more US VCs than European VCs in the sample admitted to keeping on funding poorly performing companies.

Metrics

Whilst not revealed by the main research with VCs, members of the BVCA VC Committee were of the view that US VCs have a much clearer idea of what metrics their portfolio companies need to manage in order to determine how much money to invest and continue to invest at subsequent rounds and achieve successful outcomes for their investments. VC Committee members felt that this was largely due to experience in that the US VCs have worked on many more deals than UK firms and know how to share that experience with their investee companies and advise their companies on metrics and what signs to look for:

“You call it a play book and I think they’re similar in data around SaaS and so on but they really do know and the company doesn’t spend months or ages trying to find out for themselves what the right metrics are or the right way to look at their market. The VC will have profiled them during the diligence, in discussion with the company, and it then forms part of the board material. I can say, as I look across my portfolio, you can see a difference when you’ve had one of the top funds in, earlier on, just in the quality of the board material. And that drives discipline, that drives metrics. (UK CVC*)

And so in terms of subsequent funding rounds:

“The US VCs know exactly what metrics they’re willing to fund. The reason they’re willing to put another X in is because they’ve seen that happen before. And I think the Euro guys really don’t, they’re just imputing it from what they read rather than having (the experience). (UK CVC*)

There is not the same focus on metrics in Europe:

“US investors can spot a good company from a bad company. And then the good ones they know how much money they should put in, what the valuation should be and then what you need to do to then get it to the next stage. So, that doesn’t really exist over here”. (UK VC*)

Adding value

In addition to providing finance to their investee companies, VCs usually seek to assist their companies in various ways, to add value to the financial investment and contribute to the success of the company and their investment (Hellmann and Puri, 2002; Bottazzi et al., 2008). In the sample the most common methods of adding value were helping to recruit the CEO (67% of VCs questioned on this), assisting with further financing (38%), introducing the portfolio companies to useful contacts in their networks for commercial purposes (29%) and assisting with the exit process (28%).
Table 13: Adding Value

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<th>Theme category</th>
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| Adding value (US 21, UK 24, E 13) | - Key activities are recruiting CEO and team members (67%), assisting with financing and bringing in other VCs (38%), commercial connections (29%) and assistance with exits (28%)  
- 83% UK VCs helped with recruiting cf 52% US VCs and 62% E VCs  
- 48% US VCs helped with financing cf 33% UK VCs and 31% E VCs  
- 48% UK VCs helped with commercial connections cf 13% US VCs and 31% E VCs  
- 42% UK VCs helped with exits cf 24% US VCs and 8% E VCs  
- Assisting with international expansion was not cited as value add by US VCs; only one acted as a sounding board for CEO (both more prevalent for UK and E VCs)  
- Two US VCs shared best practices with portfolio companies (no UK, E VCs cited this) |

There was less evidence of adding value activities by US VCs. This may reflect the strong screening skills of US VCs to invest in better quality companies which consequently do not need much non-financial support from a VC:

“The best companies are the ones where you add the least value” (US VC).

More UK VCs helped with recruiting, commercial connections and exits than for US and continental Europe VCs. More US VCs helped with financing than for UK and continental Europe VCs, in particular introductions to other financial VCs and to corporate VCs; a reflection of the greater supply of later-stage finance available in the US.

Exits

Despite previous studies showing that the duration of the exit stage is longer in Europe (Schwienbacher, 2008; Dantas et al., 2006), the US VCs in the sample were perhaps more prepared to wait for the most optimal exit rather than cashing out early. Early exits may result from pressure of fund raising activities to show a track record of exits.

"While in the first year or two after the financial crisis began, we were under pressure to produce cash, that then changed, and our investors are saying the priority is good returns”. (UK VC).

Investor (LP) pressure affects US VCs too:

“When you get a lot of pressure is when you’re fundraising, because... like, right now, we’re fundraising for our Fund III and people say “Well, we love your Fund II story but we’d love to see a little more liquidity out of it”. (US VC)
VCs don’t usually press for an exit unless a fund has not had any returns or there are market concerns:

“We were increasingly anxious about the market and we were keen to exit sooner rather than later”. (UK VC).

Table 14: Exit process

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<th>Theme category</th>
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<tr>
<td>Exit process (US 22, UK 22, E 13)</td>
<td>23% of US VCs wait for the best exit cf 14% UK VCs and no E VCs</td>
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<tr>
<td>36% of US VCs take proactive approach, inc appointing investment bankers cf 27% UK VCs and 23% E VCs</td>
<td></td>
</tr>
<tr>
<td>32% US VCs state companies are bought not sold cf 27% UK and 31% E VCs</td>
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36% of the US VCs took a proactive approach to achieving exits, for example by appointing investment bankers to find suitable buyers, compared to 27% UK VCs and 23% continental European VCs.

“Somebody doesn’t knock on your door that you’ve never heard of, that you’ve never spoken to, that you don’t know anything about and say “I want to buy your company””. (US VC)

Nevertheless many VCs believe in the concept that for better performing investments “companies are bought not sold”:

“We’re working to elicit unsolicited offers by doing business development with companies who might become acquirers”. (UK VC)

VCs cited an easier exit process in US (via trade sales to large technology companies and IPOs) as one of the key differences between the US and Europe, cited by 32% UK VCs, 16% US VCs and 21% continental European VCs, as referred to by Schwienbacher (2008).

Six non VC interviewees (3 LPs, 2 VC related, 1 advisor) commented on the tendency in Europe to exit from investments earlier than would be optimal to achieve the best exit (ie with a larger gain over cost), perhaps due to pressure to show investment returns to LPs in connection with fundraising but also due to not having enough money to grow large businesses:

“You’ve got to take the best offer on the table for the money that you’ve got so you’re maximising your return within the capabilities you have of limited fund sizes and that is a big issue for the UK”. (UK LP)

Pressure from LPs may also be an issue for US VCs:

“Patience is extraordinarily important in this industry and when you have limited partners looking over your shoulder saying “where is my return?” it’s easy to take that acquisition”. (US VC related)

The tendency to exit too early in Europe may be due to previous bad experience with not exiting until too late:
“I think it’s maybe the fact that they were caught out in the difficult vintages 2000 to 2002 where they didn’t exit things, there were sort of opportunities to but they tended to run more for the big 10x to 20x which unfortunately never came off and some of those investments ran out of cash and ended up being losses, so I think it’s partly having their fingers burnt in the past”. (UK LP)

Clearly timing of exits is critical and this comes down to the expertise of the individual investment executives:

“If you look at every one of our top performing funds they have established a discipline of selling that is concentrated in one, maybe two individuals, at that firm. And as an art it’s not science and these individuals just know when to sell”. (US LP)

Three interviewees (1 VC related, 1 advisor and 1 CVC) commented on the relative difficulty of achieving exits in Europe for example due to the lack of ability of UK VCs to forge contact with large US corporations. There was general agreement amongst the advisers interviewed that US Silicon Valley VCs have better contact with corporate buyers for exits. Advisers also commented that it is better to wait for a good exit:

“I think if you sort of force an exit then clearly you’re into a distress situation in terms of, upside and that, so I think, many LPs are prepared to hang in, in the interests of optimising the upside where possible”. (European adviser)

The difficulty in achieving exits may be due to the less receptive state of the stock markets in Europe for, particularly, technology listings:

“You don’t IPO your company in London unless there’s something wrong with it usually. Because it’s not an exchange that’s gonna value a high tech company”. (UK CVC)

This is borne out by the disappointing uptake of the London Stock Exchange’s new High Growth Segment, with only one company listed to date, and the lack of a pan-European stock exchange for growth companies, following the demise of EASDAQ and NASDAQ Europe, which has been put forward as a key reason for the underperformance of VC firms in Europe (Oehler et al. 2007). However Hege et al. (2009) found no evidence that the stock market environment caused any difference in performance between European and US VC backed companies. Kelly (2011) also found no real evidence that portfolio companies have suffered directly due to fragmented exit markets in Europe other than indirectly as poorly developed exit markets may discourage investment.

Wider environmental factors

Cultural differences

With the possible exception of Hege et al (2009), cultural differences between European and US VC firms do not appear to have been subject to much empirical investigation as regards the performance difference between European and US VC funds. Rohl (2016) mentions that Europe is “far behind” the US in terms of a strong start-up culture and the availability of venture capital finance and, whilst not specific to VCs, there are frequent mentions in the literature on the difference in cultures and propensity for risk in the US as compared to
Europe. There are of course many different cultures, laws, regulations and taxes in the separate European countries and vis a vis the USA. But Hege et al. (2009) found no evidence that these areas caused any difference in performance between European and US VC backed companies. Tyabji and Sathe (2011) comment that whilst VC firms in Europe operate in a similar manner to those in the US, there are important differences related to the external environments in which those firms operate, such as differences in culture and customs.

Cultural differences with regard to VC firms were discussed with the VCs and with the non-VCs. When asked about their perceptions of any differences between the environment for funds in the US and Europe 33% of VCs who commented on these differences cited cultural issues concerning the VC executives themselves in terms of attitude to risk, lack of confidence and not thinking “big” enough (cited by 47% US VCs, 23% UK VCs, 29% continental European VCs). This is perhaps summarised as a “How do I win” US attitude versus “how do I not lose?” European attitude. However this may be due to differences in the relative wealth of US VCs compared to European VCs which may permit a higher level of risk taking by US partners:

"Because all the partners have made hundreds of millions so far (in US), it’s a totally different ball game". (UK VC).

The personal wealth of VCs in Silicon Valley in particular was commented on by some of the non-VC interviewees (1 LP, 1 VC related, 1 advisor):

“There are wealthy partners in Valley: Well, they started wealthy. They were very successful entrepreneurs. They can take more risk and they can write a big cheque to start the fund”. (US VC related).

A US VC commented on the more positive approach of US VCs:

“This is a cultural thing, in California we ask the question, well if everything this guy says is true, how big can the outcome be? In Europe they ask the question, what are all the ways this guy could be lying to me?” (US Silicon Valley VC).

He went on to comment that European VCs look for every reason to say “no” to a proposition: “Europeans are saying how do I not lose and Americans look at the question how do I win?”

Culture was the area where there were the largest number of non-VC interviewees commenting on a difference between the US and European VC environments. This difference was commented on by a range of different classes of non-VC interviewees (1 LP, 4 entrepreneurs, 4 VC related, 3 advisers, 1 other, 3 CVCs) and across the countries (8 US, 5 UK, 3 E).

As for the VCs, the non VCs thought that the US has a more risk-taking, entrepreneurial, thinking “big” (eg in terms of seeking multi-billion dollar exits), open and sharing approach in the US as opposed to a more protectionist, egotistical / status driven / hierarchical focus in Europe.

This “thinking big” is not necessarily a cultural difference between Europeans and Americans in terms of any ingrained difference due to national background, schooling and upbringing but is entirely rational in view of the highly competitive market in the US:
“The reality is that people are thinking bigger (in US) but it’s not a personality issue. It comes from rationality”. (UK VC*)

The high degree of competition in the US forces VCs to “think big” and they have the financial resources to be able to back entrepreneurial companies that “think big” unlike in Europe:

“It’s not cultural, it’s not because we don’t play baseball and American football and like watered down beer. It’s actually because there are some real constraints economically and historically, historical factors and those historical factors are moving away and a legacy of closed networks of customer bases. The UK company with a great saas product can enter the US immediately. The reason they don’t isn’t because there are cultural mismatches, it’s just the competition is so high and the amount of money it’s going to take is so big and nobody’s really quite sure the milestones are what it means or access or this kind of stuff” (UK CVC*)

A South African entrepreneur in the US commented on the arrogance of Europe VCs which is not present in US VCs. This arrogance on the part of European VCs was also mentioned by a US advisor, who originates from the UK:

“One feels, with European VCs certainly again, looking back, why have returns been not so good after the last few years, that it’s a completely different mindset. When you walk in the doors of a European VC there’s a sort of arrogance: you’re incredibly lucky to receive our money, we’re very important, we’ve got very nice offices. Here, there’s a feeling very much that the entrepreneur is the customer”. (US Advisor)

Sharing

The above entrepreneur also commented on the US VCs being more willing to share. This was reinforced by a UK entrepreneur who stated that US VCs are more open, willing to talk and outgoing: “they are not so worried about what’s in it for them and are usually happy to share what they’re doing”. This willingness to share was also commented on by an advisor based in Silicon Valley:

“This country is a lot more philanthropic. People feel they want to give back and that runs through the whole Valley. People are much more protective in Europe: “I’ve got here and I’m not necessarily going to help you.”” (US Advisor)

A US East Coast VC commented on the more open, sharing culture in the US including a willingness to introduce entrepreneurs that the VC does not wish to back to other people and a non-proprietary approach to networks: “there’s a notion that if you provide help and connections that, you know, it tends to kind of flow back to you”.

There was general agreement from a number of VC related interviewees about the much higher propensity for risk in the US and the prevalence of an entrepreneurial spirit contrasted with a fear of failure in Europe:

“I think the UK venture industry has shrunk in the core, this is largely for Europe as well, has shrunk and become more conservative and it is a self-fulfilling prophecy that they put themselves into, as they’ve shrunk and become more conservative, the returns have shrunk.
They’re not taking as much risk and, therefore, the LPs have walked away in many cases” (US VC related).

This VC related interviewee went on to comment that: “When you fail in the UK, I think you, despite a lot of VCs knowing what the community says here, still turn round and go, “You’ve failed, you’re done.”

A US VC professional association executive commented: “I think that there is an entrepreneurial spirit in the US that is still lacking in many other countries. I think that more countries are getting it but the idea that failure is an integral part of the entrepreneurial process is something that is incredibly important and has been in the US, failure has not been equated with “your life is over” and I think that’s very important and basically the ability to have a huge market immediately has always been a good thing for the US as well”.

There is however much innovation coming out of Europe but this can be thwarted by a lack of entrepreneurial energy and capital to properly commercialise this innovation into successful global companies:

“There’s a thousand companies started in (London’s)Tech City. There are more graduates becoming entrepreneurs than ever before”. (UK advisor)

“There are just as many smart people with good ideas in Europe. I think there’s only just a lack of entrepreneurial capital and mindset”. (US advisor)

However, there was general agreement amongst the advisors that the entrepreneurial and enterprise culture is so much more developed in US: “and clearly in a big homogenous market place, and with Europe it’s quite different”. (European advisor)

**Fragmented markets**

Seven of the non VC interviewees (3 LPs, 2 VC related, 1 other, 1 CVC) commented on the fragmented markets in Europe with different cultures, laws, regulations, languages and politics. A stock exchange executive interviewed commented that he doesn’t see the difference in performance between US and Europe VC funds being due to the differences in practices of the firms, but more to do with the difference in size and structure of the markets which are too small in Europe, too fragmented, lacking homogeneity with a lack of mobility between countries and political differences. A UK CVC commented that:

“Most people want to start in Europe and go to America. That’s still the kind of the working assumption that you make it big in America. You don’t want to make it big in Europe. And you don’t make it big in Europe because you do actually have 27 different countries, most of which are not very rich”.

A US LP commented that: “In the US it’s easier to take a piece of technological innovation or media innovation and the whole of the US and Canada is your white space automatically. It’s just so integrated, the challenge of different cultures and different languages and how big is your market, your initial market, when you have an idea, in Europe, is a different question.
Ecosystem

Five of the non VC interviewees (2 VC related, 1 advisor, 1 other, 1 CVC) commented on the better ecosystem in the US compared to Europe including access to capital and with legal and regulatory systems more conducive to entrepreneurialism in the US.

“My perspective is that European VC is nowhere near as successful or as vibrant as US VC and the ecosystems that they sit in. And it’s not the fault or the responsibility of the VC because the VC is only one component in the ecosystem.” (UK CVC)

A UK VC related interviewee believes that ecosystem differences are the reason for the difference in performance between US and European VC funds and not operational issues or entrepreneurial attitudes, nor risk aversion which is not the significant factor that it was 30 years ago.

Regulatory and legal environments, including copyright laws, need to be more conducive to innovation in Europe. European law is less flexible than US law:

“There’s no easy way for the law to evolve with the technology without an act of parliament or an act of the European Commission. That makes innovation very difficult” (US Silicon Valley based company patent expert).

This Silicon Valley based patent expert commented that it is not possible to license all of Europe from a kind of “one-stop shop”:

“If we want to open (US company product) across Europe it takes a lot of negotiation across all the different member countries. Whilst there is now a unitary patent system and copyright across Europe the issue is who licenses it for which territory. This puts off US VCs from investing in the UK”.

Individuals interviewed by Marston et al, 2013 mentioned that copyright laws and the different jurisdictions in Europe can be a barrier to investment.

Consistent with the views expressed on exits above the financial markets are seen as being superior in the US:

“NASDAQ acts as an engine for the whole venture capital process because the prospect of IPOs at high valuations, more frequently, more easily than we can achieve in Europe, attracts venture capitalists into the field, attracts money into the field, attracts entrepreneurs to the field and so on”. (UK VC related)

“If you would have an interesting opportunity to go to the US for an IPO then just use it rather than waiting for Europe to be opening up more”. (European VC related)

Scaling issues

A number of VCs commented on the difficulty of scaling in Europe as one of the key differences between the European and US VC environments (UK 3, E 2, US 2):
“There is no single national market in Europe that is either an earlier adopter market for technology or has sufficient scale to be able to support a good sized business. Whereas, in the US you have both an early adopter market and one at scale”. (UK VC)

“The challenge for Europe has always been that we don’t have big enough home markets to build great home run returns, so companies need to be international from day one”. (UK VC)

A continental European VC commented that it is harder to scale companies in Europe as three key ingredients are missing viz: “One, a very big country where you can scale a business much faster and much more easily. Second, there can be tons of money invested in companies to scale them; and third you can find manager with outstanding scalability capabilities.

Because of the difficulties with scaling in Europe a drip-feed approach may be quite appropriate, as referred to above in the section on milestones.

“My perception is that the UK style of drip feed suits our market. Because you don’t have the same sort of scale that you have in the US so you’re more likely to lose a lot of money doing that (investing large amount of money up front) in the UK than you would in the US, because I think the market can make up for a hell of a lot given the scale of what you can go for in US”. (UK VC)

Seven of the non VC interviewees (1 LP, 3 VC related, 1 adviser, 1 other, 1 CVC) also commented on the difficulty of scaling in Europe with not enough finance available to grow big businesses. This can result in exiting from investments too early as noted in the section on exits:

“Certainly, there’s lots of evidence to say we sell things earlier but I think that’s because we haven’t got enough money to build them into truly great companies”. (UK LP)

The scaling issue can be due to European VCs not thinking “big” enough:

“X UK PE firm was very reluctant to put a huge amount of money behind something and build a global company. It was fine if it was an okay UK company, maybe international in Europe but we’re not going to build it to be a ‘global’ company. The amount of cash that the VCs are willing to put into a company here (in Silicon Valley, USA) versus Europe is dramatically different”. (US VC related)

No European market is large enough on its own to provide appropriate scale (UK CVC) and getting outside the European borders is quite complicated but: “once you’re out there we’re used to diversity so we are taking it in our stride much more easily in a way. Whereas the US can scale wonderfully in the US but find it complicated once they hit the international market”. (UK adviser)

BVCA Committee members believed that the lack of ability to scale in UK / Europe is perhaps the No. 1 issue in the difference between the UK and US environments. It is not just smaller and fragmented markets and a lack of expansion finance that is the issue with scaling
in Europe it’s also a different mindset. The mindset / thought process of US VC backed companies with regard to scaling is completely different.

“*The thought process, right at the beginning which then leads to how you develop your product, how you set your brand, what sort of people you bring in at top level, who are you targeting in terms of this region; it’s just completely different as opposed to, ‘well, let’s just get whatever sales we can and sort of figure out what we do to get bigger’. Instead, ingrained is it’s not just a great technology it is a great sort of business model that distributes that. It’s part of the mind-set. I would say very few tech companies that I see have that mentality’.*” (UK VC*)

**Technology clusters**

A number of the VC interviewees referred to the importance of operating in close networks in technology clusters, citing Silicon Valley as the outstanding example of a super successful technology hub (UK 4, E 3, US 2):

“The investments, the CEOs and their teams are just surrounded by a phenomenal ecosystem (in Silicon Valley). The connections are just phenomenal: connected advisers, connected partners. The Valley is just unique” (UK VC).

In the European ecosystem, whilst there are a number of successful technology “hot spots”, with a comparable calibre of companies and people, they are not so well developed or as concentrated as the Valley: “the raw calibre, plenty of IQ, plenty of great engineers, great ideas, all of that is just as good, it’s just that it’s so distributed that you don’t get the cluster effect, that you get in the Valley” (UK VC)

Seven of the non VC interviewees specifically mentioned Silicon Valley with its tightly networked ecosystem and culture of “giving back”:

“*Silicon Valley is very good at welcoming in people who are very giving back to the community who have something to give. It’s a very pay it forward mentality. You know, a huge number of wildly successful people spend time on folks who will never be able to repay them, right? And the intent is that those people then, in turn, as they become successful turn around and help other people who couldn’t possibly repay them*.” (US entrepreneur).

”*The mentoring, the seed capital, the giving of time and resource to entrepreneurs is something that you don’t see outside of California really*.” (UK CVC)

It is the proximity between the VCs and the entrepreneurs in Silicon Valley that helps to develop the personal networks that facilitate the investment process (Saxenian,1994; Zook, 2004). Business and personal networks are not kept separate by US VCs:

“*They’re all going out for dinner with each other every other night and sharing so it’s a very loose network of confederacy of data information*.” (UK CVC)

As referred to above VCs like to invest in technologies and / or business models that are disruptive. A US VC related interviewee commented that:
“None of the disruptive technology that’s impacting our business (changing the world) is coming from anywhere else but Silicon Valley”.

Three non VC interviewees (1 LP, 1 entrepreneur, 1 VC related) commented on the huge added value that Silicon Valley VCs can bring to their portfolio companies through their extensive networks:

“US (West Coast) VCs use overwhelming force in supporting a project. And I don’t just mean dollars of overwhelming force, but connectivity and networks and relationships with big corporates. Europe is not able to efficiently filter the ones that will gain traction from those that won’t. The vast majority fail to gain traction”. (UK LP)

“The reason we took money ultimately from the Silicon Valley guys was that we were expanding fast in America and just felt that they could help us leverage the situation and Kleiner had a lot of experience of building or backing consumer facing businesses in the US (including Amazon and eBay)”. (UK entrepreneur).

Zhang (2007) comments on the better access to venture capital in Silicon Valley with start-ups receiving more finance at an earlier age, with more rounds of financing and more money in each deal.

The relative “uniqueness” of the Silicon Valley VCs and the environment in which these firms operate was a common theme arising from the interviews. Reference was made to the outlier performance of some Silicon Valley based firms, the operational and/or entrepreneurial background of investment executives, the more risk-taking approach of Silicon Valley firms, the disruptive technology that comes out of Silicon Valley, the brand strength of well-known Silicon Valley based firms which helps to attract the best deals and the best LP investors, the entrepreneurially friendly terms provided by West Coast VCs, the better contact with corporate buyers for exits and the trend to syndicate with fellow VCs at the earliest stages of company development to get a “foot in the door” with potential home-run companies. Reference was also made to the huge added value afforded to portfolio companies through the extensive networks in the Valley plus the non-proprietary willingness to share time and resource in a “giving back” culture in Silicon Valley.

Some Silicon Valley based firms have superior fund performance, though this is by no means exclusive to the Valley. Of 6 firms with funds with outlier performance of greater than 50%, 3 of the 5 US firms included therein were operating out of Silicon Valley. Of the 12 firms which had two or more funds with top-quartile performance, 4 of the 7 US firms in this category were operating out of Silicon Valley. The characteristics of Silicon Valley based VC firms referred to above may well contribute to this better performance.

The success of Silicon Valley has led policy makers to attempt to “clone” in other geographies (Rosenberg, 2002). It is however difficult to replicate the unique culture and ecosystem of Silicon Valley elsewhere, including in Europe:

"The European Union, or the countries here in Europe, they look with envy at Silicon Valley and try to recreate it; not always by doing the right things because sometimes they just throw money at anything without thinking too much about the consequences of that”. (European CVC)

“Due to the fragmentation of countries in Europe with their own policies etc it’s very difficult
to create a technology cluster with critical mass. None of the clusters like the triangle of Cambridge, Oxford, London or Heidelberg or Sophia Antipolis has really taken off”. (UK VC related)

“I think the single hardest thing for the UK and Europe to do is replicate a culture. Culture is really hard stuff because it’s squishy and soft”. (US VC related)

“I don’t think taking a Silicon Valley style of investing, which depends on a clustered ecosystem, and just plopping it down on top of Europe is going to work”. (UK VC)

**Lack of experienced CEOs and serial entrepreneurs**

A lack of good CEOs, serial entrepreneurs and people with sales & marketing skills was cited as a key difference between Europe and the US by 31% of the VCs interviewed (41% UK VCs, 26% US VCs and 21% continental European VCs). Axelson and Martinovic (2013) state that a contributor to the difference in performance between European and US VC funds is due to serial entrepreneurs being less common in Europe.

A Silicon Valley based VC with operations in both US and UK commented on the reasonable number of good CEOs in the Valley and the relative lack of them in Europe:

“That’s been our biggest challenge in Europe is finding someone that can really run a startup and take it to success”.

This was confirmed by a UK VC who commented that in Europe management is at a premium: “people who have done it before and know what they’re doing”.

A UK VC was disappointed by the quality of candidate CEOs: *I wouldn’t say the quality is as high as it should be. I think the UK needs an upgrading across the board.*

A continental European VC agreed that the pool of experienced start-up management is generally larger in US, but with the considerably lower amount of VC in Europe relative to the US:

“I would still state that it is at least that easy to find good management as it is in the US because we need only one fifth of the number of good CEOs like in the US”.

However in his view it is the established networks to pull the right CEOs into the right situations in an efficient and quick manner that is missing in Europe.

A US Silicon Valley VC stated that not having enough really good CEOs in Europe is effect and not cause: “you have fantastic managers in Europe, it’s just that they don’t quite take the gamble to go and work for the start up yet because there haven’t been enough cases to follow”.

A shortage of software engineers in Europe was also seen as an issue:

“For the last 15 years most of Europe, but particularly the UK, hasn’t really stimulated and motivated people to come out of university with engineering degrees particularly in software. And today, software companies are the ones that are the most financeable, that arguably has
the biggest upside that arguably is going to do the more dramatic things”. (UK VC)

Comments were made about the difficulty in recruiting the right quality of sales people in UK, both strategic marketing, business development and “out and out sales guys who can make 20 calls, get 5 meetings and make a close”:

“Sales in the UK, I think, are still seen as a bit of dirty... you know, it’s not really a profession”. (UK VC)

A number of the non VC interviewees in this study commented on the lack of experienced CEOs (2 VC related, 2 advisors, 1 CVC) and serial entrepreneurs (3 VC related, 2 CVCs) in Europe:

“I think Europe is getting there but we didn’t have that initial, we don’t have that large enough base, yet of entrepreneurs and CEOs that have done it before”. (UK CVC)

“We’re starting from a small pool of CEOs; not as good a track record and therefore lack self-confidence. Not many CEOs, even the good ones, have been through a $1bn IPO”. (UK adviser)

“A lot of the best entrepreneurs have left the UK to come here (Silicon Valley) because they are “p....d off” at trying to raise money in the UK”. (US VC related)

There was general agreement at the tendency in Europe for an entrepreneurs to retire if they have made money and not go on to start other ventures or become super angels as in Silicon Valley:

“I still have to see I must admit, this kind of billionaire former entrepreneur, turned billionaire, turned super angel in Europe. I haven’t seen that many examples, if I’m honest”. (European VC related)

“We don’t have the cycling around as much of the entrepreneurs as they do in the US”. (UK CVC)

Maybe this is because of the harsh conditions that the entrepreneurs have faced in Europe:

“In my view a big factor in Europe, we finance companies so poorly when we make life conditions of entrepreneurs seem so bad by the time they’re done with the start-up, three or four years or five years later, they’re exhausted and say ‘why on earth would I want to go through that again?’” (UK advisor)

Luck

Eight VCs mentioned luck as an ingredient of their success with investments (UK 5, E 1, US 2).

A Silicon Valley VC agreed that luck has a “huge amount to do with it”. An East Coast US VC did not disagree that luck is important including being in the right place at the right time:
“We effectively live in non-predictable, fast-moving, chaotic environments, so luck plays a big part”.

A UK VC clarified this as follows:

"You can be at the right place at the right time because you are lucky and luck helps but who was it said “the more you practice the luckier you get”? So, I think actually, forethought is what enables you to be lucky enough to stand in the right place at the right time”.

As did a continental European VC:

“I mean you can dress that up and say well we got lucky with that investment and we probably did to some point but again you kind of have to be in a position to take advantage of getting lucky”.

Finally a number of non VC interviewees (3 LPs, 1 entrepreneur, 1 advisor, 2 others, 1 CVC) commented on the part luck plays in investment, and therefore, fund performance success:

“If there were UK managers who had serially successful funds, I’d say it wasn’t luck, it was the skill of the managers, but there have been too few serially successful funds”. (UK LP)

“I would say an awful lot of it is luck. That they happened to find Google, Yahoo, Pinterest, Facebook, right? Very, very early on, right? Once you’re lucky, twice you’re good. But I think a lot of that is just a matter of placing a lot of big, risky bets”. (US entrepreneur)

“I’d always say luck is important but preparation is important as well. It’s amazing how many people who are lucky are well prepared”. (US university professor)

Skill in the investment process is of course absolutely crucial to success. Whilst luck might play a role in the investment process, Gompers et al (2006) argue that a major component of success in both entrepreneurship and venture capital can be attributed to skill.

Practical implications and sharing of best practices

For the sample of VC firms included in this study a number of areas where the investment practices of European VC firms differ from those of US firms have been revealed that do not appear to have been extensively addressed in previous research. In particular the adoption of a high risk, “1 in 10”, home run investment strategy by many US firms included in the sample with some US firms pursuing outlier deals at the behest of a senior partner without necessarily the consensual approval of the partner team, the use of “entrepreneurially friendly” terms in the term sheets of US West Coast based VC firms compared to the more “investor friendly” terms favoured by many European and East Coast based US VCs, the “theme” approach to identifying hot areas for investment used by several US VCs, the benefit “brand name” VCs, particularly in Silicon Valley, obtain for deal sourcing and the greater local sector knowledge and deep networks of US VCs that aids in-house due diligence and targeted exits. There is also some evidence that US VCs may hold onto investments until more valuable exits can be achieved, contrary to previous research showing that US VCs exit earlier than European VCs (Dantas et al, 2006).

Whilst it is not unequivocally possible to link the observed differences in investment
practices from this study to the difference in performance between European and US funds it is clear that the sample of VCs investigated does exhibit a clear supremacy of performance overall by the US VCs included in the sample. The different investment practices may well contribute to this difference, along with various cultural and economic differences to which much reference has been made by the interviewees (of these the more open ecosystem in the US and a willingness to share talents and information, in contrast to a more proprietary culture in Europe, are particularly noteworthy). This study has worked with a purposive sample of 64 separate VC funds in Europe and US and a sample of 40 additional stakeholders, which is satisfactory for qualitative purposes. However it does mean that the findings from this study cannot be extrapolated to the full population of VCs and related stakeholders.

It is well known that US VC funds are on average larger than European funds and employ more partners in their teams, characteristics that are also borne by the funds included in this study. The research is consistent with anecdotal evidence that US VC firms have proportionately more partners with operational and, to a lesser extent, entrepreneurial backgrounds, than European firms. This may well assist in the screening and value-adding capabilities of US VCs which could contribute to the performance difference.

Whilst the performance difference may also be due in part to differences in wider economic and possibly cultural factors, together with such areas as the drive and ambition of entrepreneurs and the number of investment opportunities pertaining to the different geographies (Lerner et al., 2011), a possible implication of this study for the UK / European venture capital industry is that UK / European VC performance could potentially be improved by considering the adoption of certain investment practices of US VCs as discussed in this report.

“There is a big difference between performance and it’s not just in the absolute returns, it’s in what entrepreneurs think the value add has been. US firms are more aggressive, they’re looking at the “Babe Ruth” approach, European firms are far more timid and that comes out in everything the entrepreneurs say”. (UK CVC*)

UK environment

With specific regard to the UK, whilst there remains a significant difference in performance between UK and US VC funds, there are many excellent features about the venture capital sector in the UK. These include adequate finance for early stage investment, many accelerators and a higher number of interesting companies coming through for series A and B investment, the formation of the British Business Bank, much technological innovation from the universities, centres of excellence in artificial intelligence, fintech and other areas, more people studying entrepreneurship and joining entrepreneurial companies and several more recently established UK VC firms that are operating along US Silicon Valley lines:

“These are the new kids on the block and they are so different and they’re driving a lot of this business”. (UK CVC*)

Sharing of knowledge and information, as is prevalent in the US, will hopefully improve:

“I just find investing in Series A, B stage significantly better than it used to be. The amount of experience and exposure is a lot greater than it was, I think. As long as people are
reasonably open about what’s working and what’s not working there will be a sort of shared pool of knowledge and it will improve”. (UK VC*)

However, there is more that can be learned from the US VC sector to make the environment for UK VC even better. US firms are more aggressive, they’re looking at the “Babe Ruth” (swing big) approach. UK, and continental European firms are far more timid. This is not a cultural issue. It’s due to real economic factors, including a more competitive environment in the US and issues with scaling, fragmented markets and a lack of later stage finance in Europe.

Best practices

Whilst it is generally accepted that European VC needs to improve there are considerable economic and practical issues and constraints to UK / European VC firms adopting the US VC practices as discussed in this research.

“There are quite a few things in there (in the research) that would be nice to think that we could cookie cut but you can’t. I talk a lot to other VCs and US VCs, and it’s not that no-one knows it because we all know instinctively that it needs to shift a gear but, actually, when it comes down to the nuts and bolts of getting the deals done through the partnerships and pleasing LPs and raising another fund, a lot of the high-minded nice intention ends up giving way to pragmatic realism”. (UK VC*)

Nevertheless there are certain measures that could be considered.

A key aim of this report is to encourage debate and discussion on these areas and on the constraints to their practical implementation.

UK and continental European VCs could consider adopting:

- more of a higher risk, “home run” investment strategy where considered practical and rational
- the pursuit of outlier deals championed by senior, experienced partners
- the use of “entrepreneurially friendly” terms and less focus on the downside
- a “theme” approach to identifying hot areas for investment
- raising larger funds, where practical, for follow-on funding and scaling
- hiring partners with operational backgrounds
- exiting from investments when the most value can be achieved, depending on market conditions and scaling potential
- a less proprietary approach, more networking and sharing of information including dissemination of best practices
- building collegiate syndicates
- focus on data and metrics that drive investment decisions which drive operating decisions
- focus on medium to long-term milestones.

In addition there is the need for more receptive public markets for technology companies, with better understanding of technology, eg for SaaS companies, together with a ready supply of good CEOs and entrepreneurs willing to form serial ventures.

Adopting the above practices and environmental conditions for VCs in the technology clusters in Europe might effectively mirror those operating in Silicon Valley. Policy makers
have attempted to “clone” Silicon Valley in other geographies (Rosenberg, 2002) with limited success. Creating Silicon Valley type VC environments in Europe will not just require money, though more follow-on and later stage financing for high-growth technology companies will be required. As extolled by one of the VC related interviewees in this study, government support and incentives for clusters will be required with more technology R&D taking place via government and military sponsored research:

“Government sponsored research is a huge multiple in US compared to Europe. Governments have got to give incentives for creating clusters. Government has to provide incentives for investors to get into early stage. We need a revival of technology R&D here in Europe via the military, EU and government sponsored university research”. (UK VC related)

It will also be crucial to have clusters that are more interlinked and networked than operate currently in Europe and also a change in culture on the part of European VCs with more risk taking, more “thinking big”, more mentoring, sharing and giving back.

Improvement in VC performance, potentially by adopting these recommendations, could encourage greater investment into the sector by institutional investors leading to improved opportunities for financing the potentially high-growth companies of the future in Europe.

Concluding comments

The performance of European VC funds on average lags behind that of US VC funds and this has led to less investment into European VC funds by the traditional non-governmental investors which in turn means there are potentially less monies available for investment into high-growth entrepreneurial companies in Europe. This study has investigated differences in investment practices between European and US VC funds, and in the environments in which they operate, which may go some way to explaining the performance difference.

Views of VCs and those related to the VC industry (the “non VCs”, including limited partner investors, entrepreneurs, advisors and corporate venturing investment executives) were ascertained which is possibly the first time that the views of VC and non-VCs have been expressly compared with regard to the performance difference. There was much agreement between the sample of VCs and the sample of non-VCs included in the study as to the categories within these areas that could be responsible for the performance difference. The study also showed considerable agreement between the different classes of non-VC as to the differences between Europe and the US.

Whilst the UK / European VC environment is improving it is hoped that this report will generate further discussion by the industry and others, including LPs and entrepreneurs on the areas raised in the report and encourage the sharing of best practices within the industry.

Readers are encouraged to submit their comments to the author of this report at: keith@keitharundale.com

The author is keen to follow-up this research with further in-depth interviews with VCs and others interested in this area.
List of references


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