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Functions of venture capital in business management

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DESCRIPTION

Venture capital helps entrepreneurs through the capital-raising process and provides targeted, quality deals to its network of investors. Venture Capital also equips the venture capital community with the tools needed to make the investment process and business development easy and efficient. These tools include a clearinghouse that provides valuable, direct industry connections; a supportive community based on common experiences; the latest market news across the globe; and access to a high-quality network of professional service providers. Technological change and development is one of the most important ingredients of economic and social development. The encouragement of the birth and growth of high technology firms is a major factor on which the survival and growth of any economy may depend.

Many developed countries realized quite early the role of new technology industries as the key factor in determining the national economic success. They took all the measures to encourage the rate of formation of new firms and their subsequent growth. The essence of any economy is the small and medium enterprises. Several processes cannot be put into commercial operation because of the latent high risk and uncertainty involved in their successful production and marketing. Rational investors normally avoid such investments. In such a situation venture capital financing assumes greater significance.

Venture capital financing acts not only as a financial catalyst but also provides a strong impetus for enterprises to develop products involving newer technologies and commercialize them. It is well known from the success stories of a few giant corporations like Digital Equipment Corporation, Apple Computer Inc., Federal Express, Staples Inc., Genetic Institute, etc., that venture capital has played role in their birth and growth. In the last fifteen years, venture capital has emerged as an important area of finance for academic researches. Since its inception after the Second World War, venture capital has had little known but profound impact on the U S and World Economy. It has played a catalytic role in the entrepreneurial process: Fundamental utility that triggers and sustains economic growth and renewal. In terms of job creation, innovative products and services, competitive vibrancy and the dissemination of the entrepreneurial spirit, its contribution has been staggering. The new companies and industries spawned by venture capitalists have changed the way, in which we live and work.

Venture capital has become an increasingly important source of financing for new companies, particularly when such companies are operating on the frontiers of emerging technologies and markets. It is a significant innovation in the twentieth century. It is a form of equity financing especially designed for funding high risk and high return projects. Venture capital implies investment in a project where the uncertainties have yet to be reduced to risks. When many entrepreneurs are with good project ideas but without adequate funds to commercialize them, venture capital can open new avenues for such entrepreneurs. It plays an important role in financing high technology projects and helps to turn research and development into commercial production. Besides financing technology, venture capital is also involved in fostering growth and development of enterprises. Venture capital means funds invested in small and medium high risk firms which give a risk of total loss and an opportunity for very high returns that are founded on commercial applications of some technological innovations. These investments are made in new business based on tested technology that is being transferred to new markets.

Venture capital investments are categorized by different stages in financing of the firm such as seed capital; start up, expansion and development financing prior to going public. The concept is basically of U.S. origin where it has achieved a tremendous success. Venture capital can be traced back to four decades when George Doriot, the father of venture capital and Rockefeller family provided finance to companies making use of new technologies. The real development of venture capital took place in 1958 when the Small Business Investment Act was passed by the U.S. Congress to license the companies and provide venture capital, tax incentives and government loans etc. These companies were known as Small Business Investment Companies (SBICs). In UK, it received a boost by way of the Government's Business Expansion Scheme which permitted individuals to claim tax reliefs for investment in companies not listed on the Stock Exchanges.

The American experience prompted the Japanese to adopt the concept. Now, Japan is experiencing an entrepreneurial and venture capital growth as a traditionally homogeneous culture attempts to learn what makes innovation work in the U.S. In the eighties, a number of' Asian countries established venture capital firms and the Governments have been playing an important role in their development. Risk capital, in India, has always been in short supply. In order to provide this, Public Financial Institutions have been set up. They have played a catalytic role in the development of industry. Nevertheless they did not venture out on expected lines, but were contended to give debt finance, mostly in the form of term loans to the promoters and their functioning has been akin to that of commercial banks.

The first generation entrepreneurs found it difficult to raise equity even to the extent of promoters' contribution to be brought in by them. To partially mitigate the sufferings of such entrepreneurs, All India Financial Institutions came out with novel schemes like seed capital scheme, risk capital scheme, etc. But the problem of equity finance for new untried enterprises remained unsolved. Further those Indian banks and Financial Institutions have been extending finance based on the principles of' safety. Security, liquidity and profitability of the assisted units has necessitated the setting up old venture capital firms during the later part of' the eighties. In public sector, Industrial Credit and Investment Corporation of India and Unit Trust of India jointly set up Technology Development and Information Company Ltd. In 1989 for providing venture finance (now known as ICICI Venture Funds Management Company Limited). In recent times more number of Venture Capital Companies Funds has been set up by commercial banks, private sector units, state financial institutions and foreign companies.