Beyond V2C: Entrepreneur's Risks and Returns in the Era of Networked and Global Business

Jukka Ala-Mutka[1]; Hamid Etemad[2]

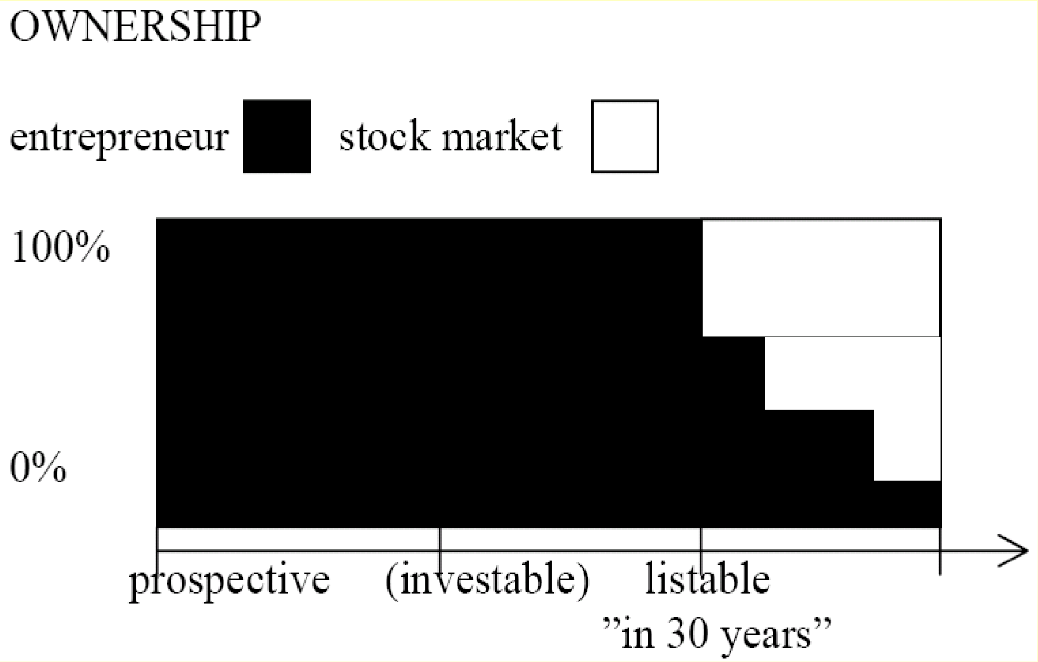
*[1]**DSc, Helsinki School of Economics,** Finland*
(jukka.ala-mutka@hse.fi) and
*[2]**PhD, McGill University**, Canada*
(hamid.etemad@mcgill.ca)

Research Question: SMEs and Consistent Rapid Growth?

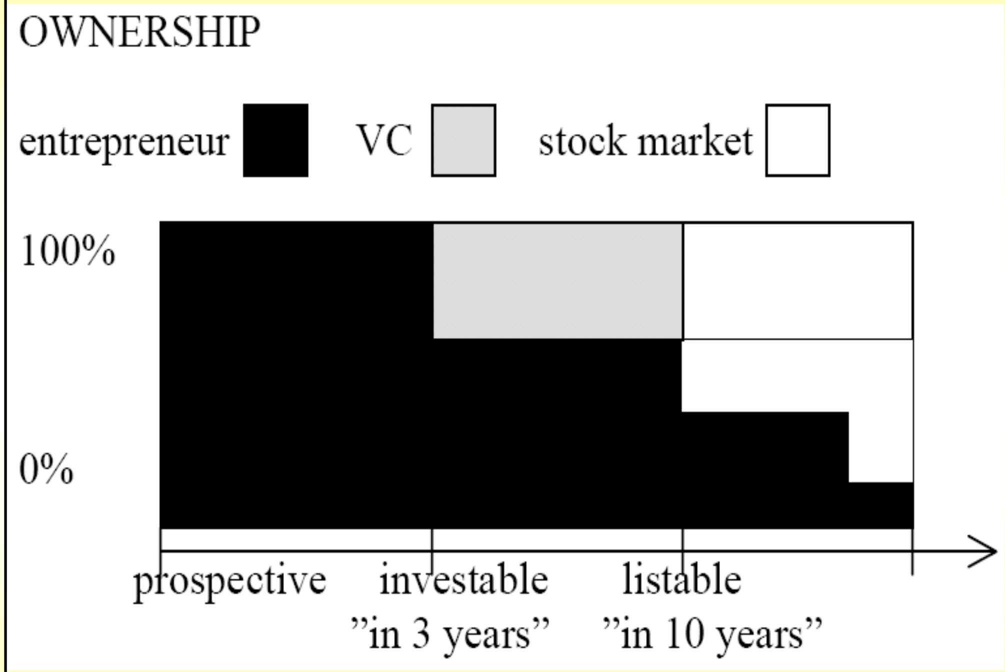
- When firms are resource-deprived, relatively young, inexperienced and at the earlier stages of their life cycle, at least three families of questions are not clear:
  - i) which **factors** are present and influential,
  - ii) **how** are they brought to bear at the early stages of a young firm's life-span, and
  - iii) which **combination** of factors can put the younger smaller firms on the higher growth paths, especially

- **Enduring Great Company?**

Playing Solo

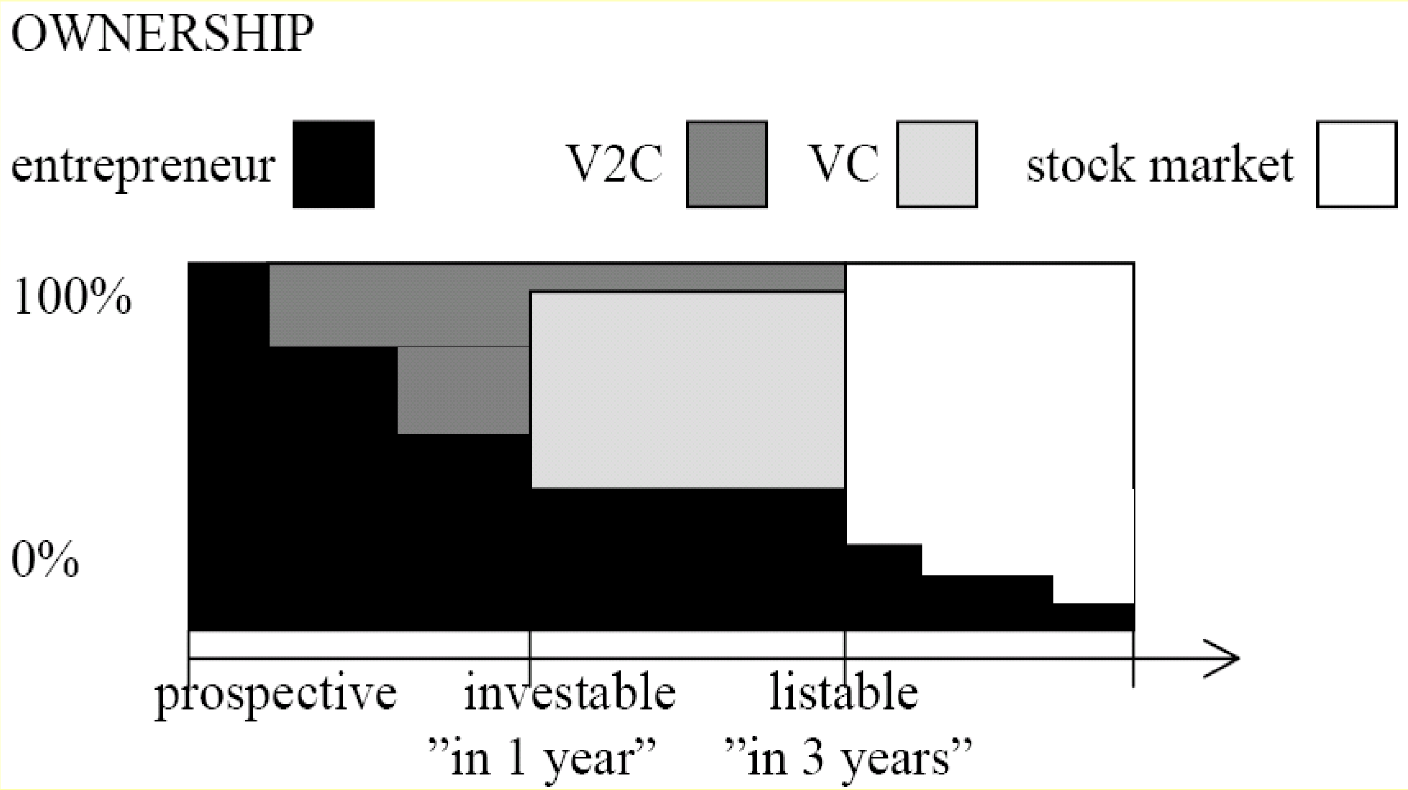


Pushed by Venture Capital



Source: Seppä & Näsi 2001
Also Rasila, Seppä & Hannula 2002 and Rasila 2004

Accelerated by V2C



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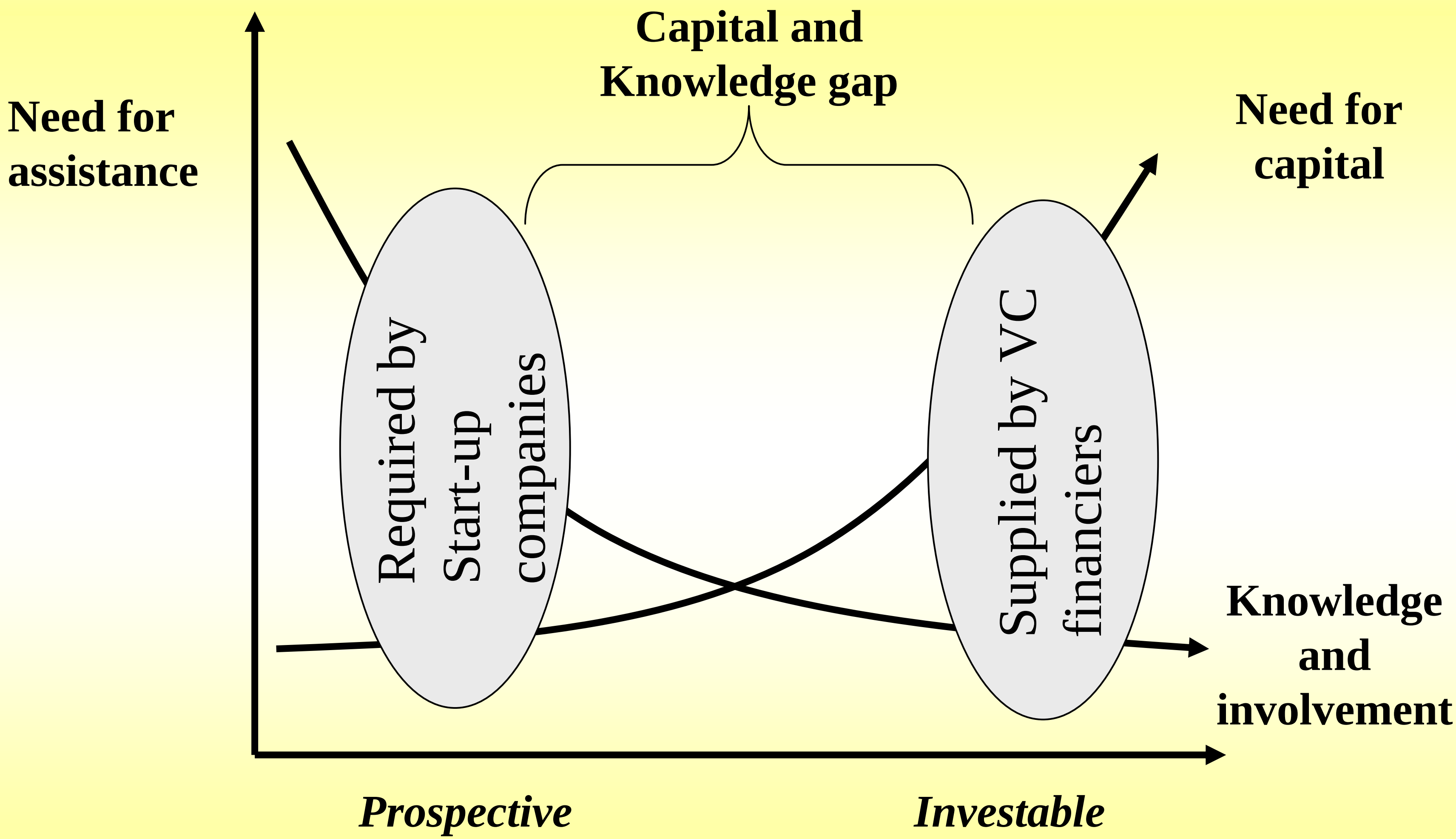
A Summary Highlights of the Selective Characteristics of the Studied Case-Firms

Company Name	Five year growth rate	Revenue 2005 Canadian $	Foundation	IPO or Listing
1.AirIQ Inc.	**3,014%**	$40 million	1997	2001
2.Carmanah Technologies Inc.	**3,669%**	$39 million	1997	2001
3.DTI Dental Technology Inc.	**2,570%**	$35 million	1996	1999
4.Extreme CCTV Inc.	**12,735%**	$24 million	1994	2002
5.Garda World Security Inc.	**9,452%**	$259 million	1994	1999
6.Pethealth Inc.	**8,306%**	$14 million	1999	1999
7.TLC Vision Inc.	**28,938%**	$303 million	1993	1997
8.Western Financial Group Inc.	**9,647%**	$64 million	1996	1996
Average			1996	1999

3,5 years

The Knowledge and Information gap



Source: Rasila, Seppä and Hannula 2002

Gap Reduction Approach

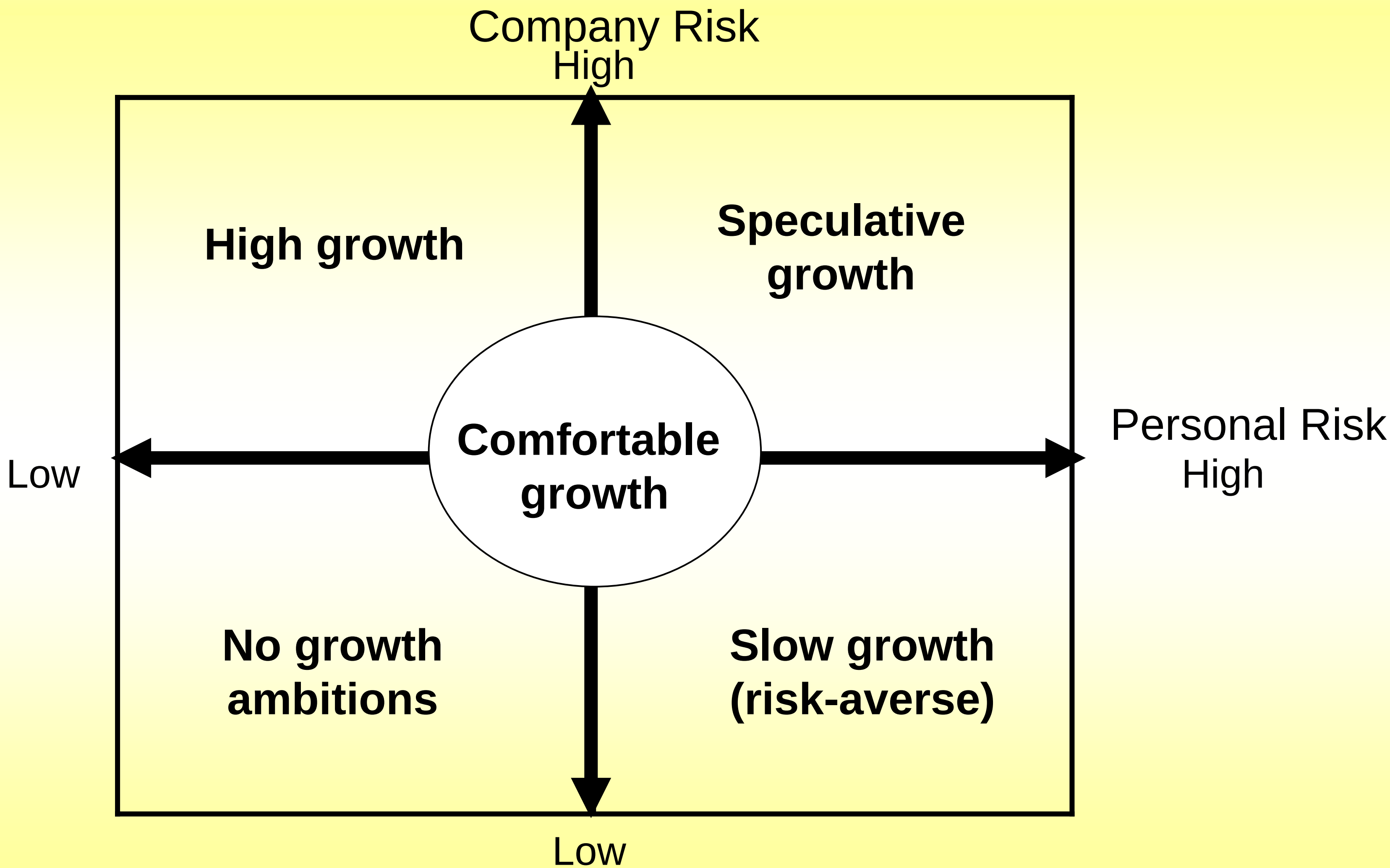
- **Entrepreneurial-Managerial Gap**
  - *Shortcomings in both the mindset and the required qualities of the starting entrepreneurs in the beginning for the growth venturing to proceed (Penrose 1959, Kotter & Sathe 1978, Covin & Slevin 1997, etc…)*
- **Resource-Capability Gap**
  - *Equity Gap (Rasila, Seppä and Hannula 2002)*
  - *"It is ironic that there is no shortage of capital now; but there is a shortage of small-enough doses of it" (Seppä & Näsi 2001)*
- **Information-Knowledge Gap**
  - *Knowledge Gap (Rasila, Seppä and Hannula 2002)*
- **Structure-Governance Gap**
  - *"A structure-conduct-governance" paradigm, where the changes in equity capital or ownership structure influence the governance principles of the enterprise (Ala-Mutka 2005)*

Source: Etemad & Ala-Mutka 2006

The Entrepreneurial Choice

- Historically, entrepreneurs have **created jobs for themselves** and family members, employment for others, and their regions as a whole gradually.
- Successful **family firms**, such as Medici’s, Farnese, Della Rovere’, Rothschild’s, Armstrong’s, Chippendales and Parsons, Ford, Carnegies and Rockefellers...
- Creation and preservation of **family wealth** has been the primary objective over time
- **Serial or “professional”** entrepreneurs and **co-entrepreneurs**
- The choice in the selection of entrepreneurial **team**

Four States of Personal-Company Risk Trade-Offs Based on the Range of The Entrepreneurial Choice



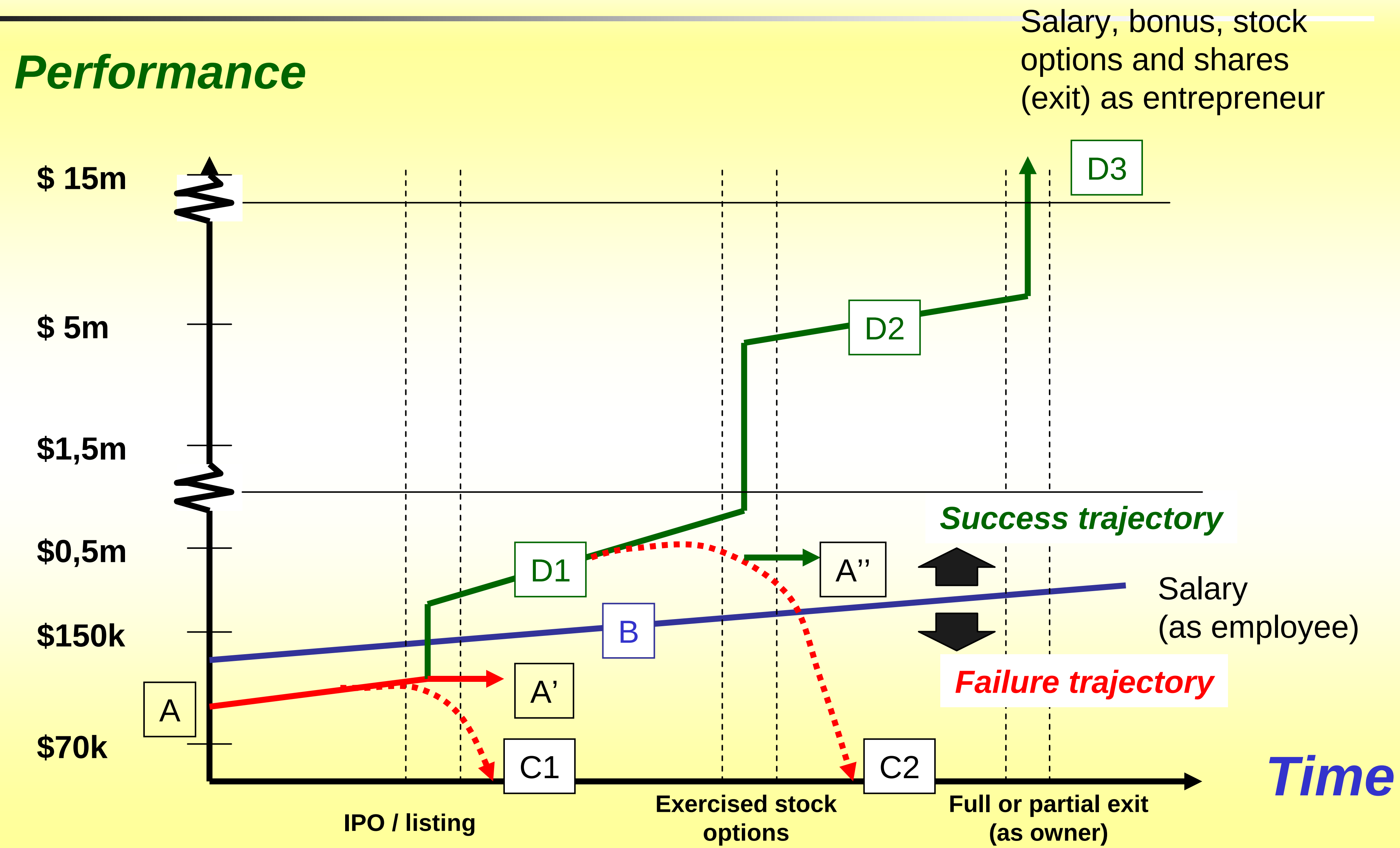
Findings #1: Returns of Entrepreneur

- Average salary **$101,000** of senior executive in Canada
- Average compensation **$288,00** (Profit Listed growth companies)
- Year before IPO: top executives earn same than average SME executive
- Year after IPO: **$286,000** and median $195,000
- Fifth year after IPO: **$350,000** and median $279,000.

Examples

- Founder-director of TLC Vision Inc. **$850,000** per year versus average annual income of $140,000 for typical doctors in Canada
- Founder and CEO of TLC Vision inc. with BBA Certificated Accountant was **$450,000** per year vs. average salary for CAs with approximately 10 years' experience of $104,000
- Garda's founder-CEO annual compensation were $135,000 in third year after listing and **$883,000** in sixth year.
  - In 2005 Non-exercised options value **$4 million** (300 000 shares).
  - 4,9 million shares (19 %), at present stock value **$110 million**

Findings #1: Personal View to Success and Failure



Findings #2 Risk of the entrepreneur and firm

i. The founder's average ownership share declines from **35%** before listing to 21% in the year of IPO and to less than **14%** in five years after IPO (median 10%).

ii. At the same time, they lowered their personal risks as well as company risks when they capitalize their "entrepreneurial capital"

iii. The firm had raised funds from VC or stock market via IPO and private placements as early as possible.

- VC's role was more important in the seed and start-up stages, became less important in the **real** growth stage.
- At the high growth stage the ventures were able to raise funds from banks as the earlier success worked as collateral.
- Funds from banks were certainly cheaper than those from VC ("for example, 6,5 % interest rate from Bank than 12 % from VC")

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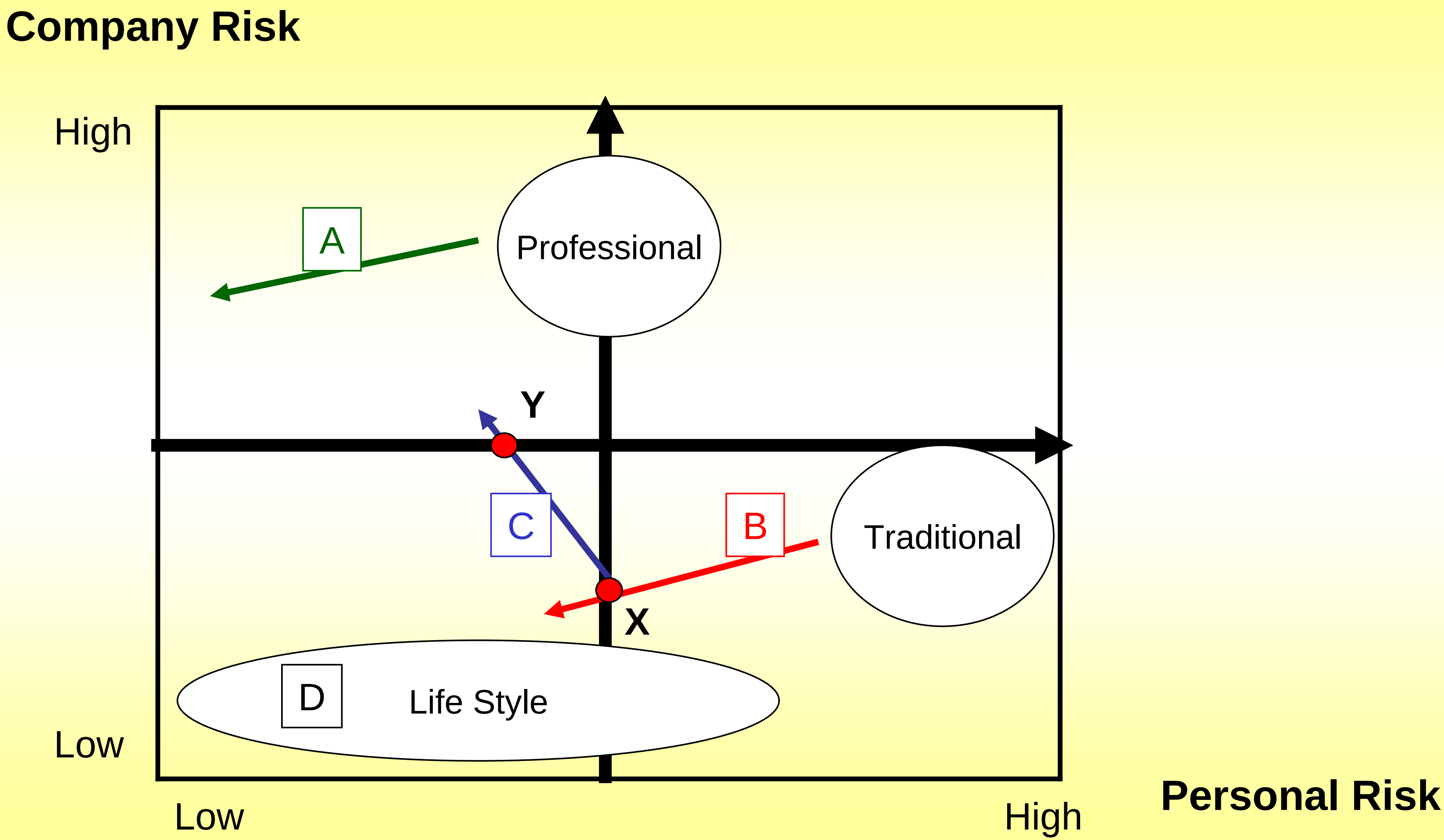
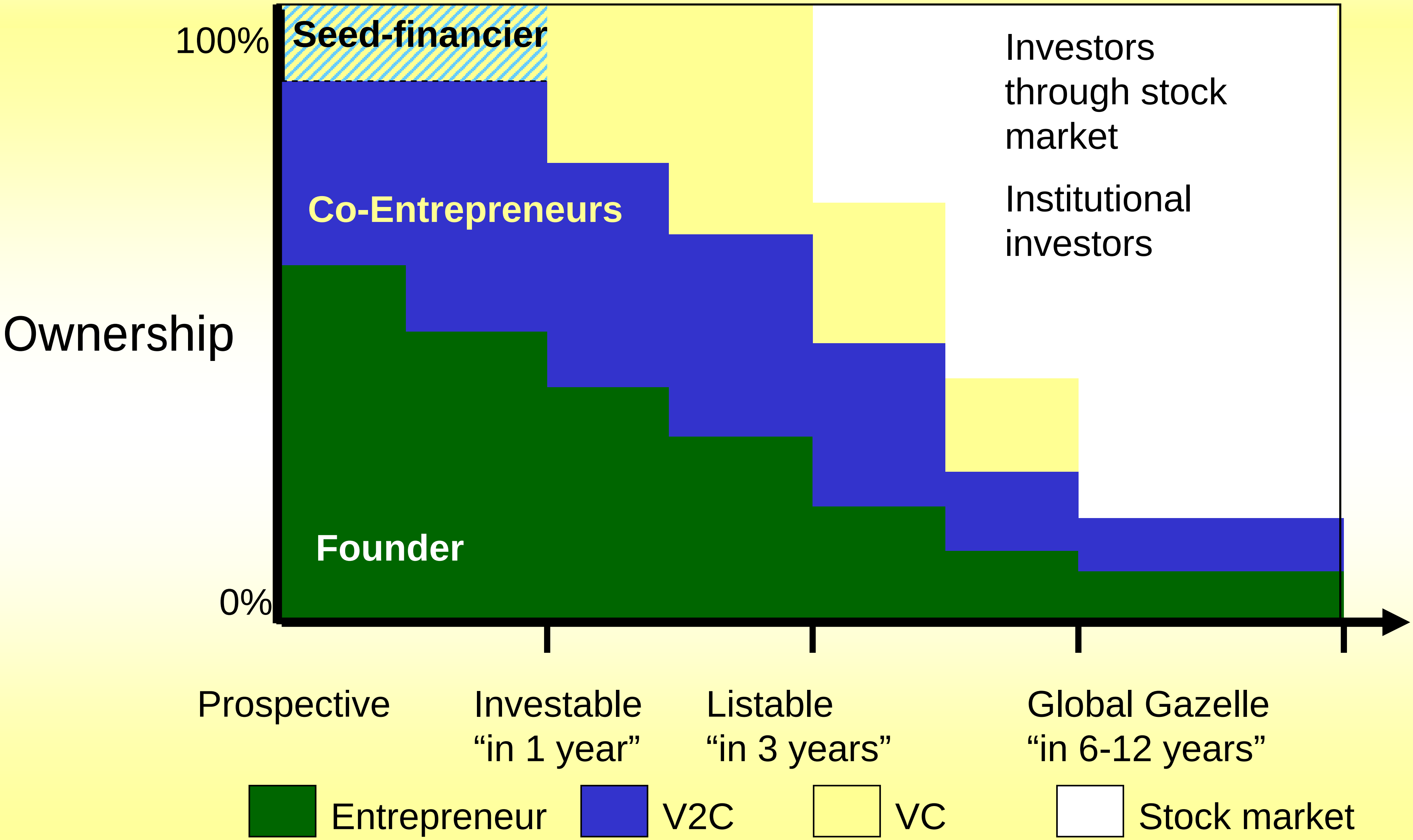


Findings #3 Towards Venture-to-Growth model (**V2G**)

i. Expand their ownership-base earlier;
ii. Go public early-on and;
iii. IPO is not the main exit route for entrepreneurs, V2C actors or even venture capitalists (VC).

- IPO and listing on stock exchanges seem to be a working mechanism for early stage financing, **incremental and partial exit** for all stakeholders, incentives for entrepreneurs and V2C actors and a measure of early, but not the ultimate, success.

Findings #3 Towards Venture-to-Growth model (**V2G**)



Findings #3 Towards Venture-to-Growth model (**V2G**)

- Founders **reduce their personal risks** by exchanging part of their ownership stake for higher salaries, stock options and partial exits during the growth.
- Founders will gradually face **similar incentives** to those of the co-entrepreneurs as well as the hired managers
- Support long-term commitment and the separation of the key roles: **manager, director/board member and owner**
- This evolution is actually required by the formal and **institutional investors**
- It resonates with **good governance principles** requested by stock exchanges.
- The **Structure-Governance-Paradigm** is fundamental element of the rapid growth ventures beyond V2C.

V2G model points out three proposals

1. it examines risks and returns from entrepreneur's **individual** viewpoint
2. it explores risks and ambitions **between individual and enterprise**
3. it describes the importance of the **ownership development** of the enterprise and development of the value of the enterprise

Thank You!
Questions?

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Growth path of Garda World Security Inc.