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The exit decision in the European venture capital market

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This article analyses the exit decision in the European venture capital market, studying *when to exit* and how it interacts with the *exit form*. Using a competing risks model we study the impact on the exit decision of the characteristics of venture capital investors, of their investments and of contracting variables. Our results reveals that the hazard functions are non-monotonic for all exit forms and suggest that, in Europe, Initial Public Offering candidates take longer to be selected than trade sales. Moreover our results show that, in Europe, venture capitalists associated with financial institutions have quicker exits (stronger for trade sales), and highlight the importance of contracting variables on the exit decision. An unexpected result is that the presence on the board of directors leads to longer investment durations.

Keywords: Asymmetric information; Venture capital exit decision; Trade sales; IPO; Write-offs; Competing risks model

JEL Classification: C24, G24, G32, G38, K22

1. Introduction

Although there exists a significant literature on venture capital investment, the most part it is related to the initial and business development phases of the investment. There have been relatively fewer works on the divestment decision. Most of the existing studies on the exit decision focus on Initial Public Offerings (IPOs). This is explained by the fact that IPOs are the exit form which is more relevant in the US and the one associated with higher returns. In addition, the information on IPOs is easy to obtain, which facilitates empirical analysis of the subject.

In the particular case of Europe, where trade sales are the most important exit form,§ the study of the venture capital exit decision has been even more neglected. This paper analyses the divestment decision in the European venture capital market using data obtained through questionnaires. We study two important dimensions of the exit decision: *when to exit* (the duration of the investment) and *how to exit* (which form of exit to use). These two aspects of the exit decision are interrelated and therefore they should be studied together.¶ However, the literature on the exit decision has analysed either the duration of the investment or the exit form, with the notable exception of Giot and Schwienbacher (2007) who consider simultaneously the two dimensions. Our paper is another contribution in this direction since we explore the interactions between the two dimensions of the exit decision. The main contributions of our paper with respect to Giot and Schwienbacher (2007) are the study

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§According to EVCA, in 2010 trade sales represented 23.7% of the total amount divested while IPOs represented only 11.8% (considering the amount divested by country of private equity firm). In 2005, the last year in our data, the percentages were 22.6% for trade sales and 9% for IPOs.
¶Schwienbacher (2010) argues that both dimensions can affect the value of the investment and the incentives of the venture capitalist and the entrepreneur in adding value.