



Selected Proceedings from the 2000 annual conference of the International Leadership Association, November 3-5, Toronto, Ontario Canada

Leadership and Start-up Financing

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Leadership rightly is associated with the presence of followers, but the traits associated with leadership are desirable in non leaders as well. Indeed, one could argue that a good leader is one who develops such traits among his followers, making himself dispensable and even redundant. This argument is appealing in principle, but it also has grounds in the practical wisdom of business (as opposed to management) where the goal of every capitalist is to set up one source of cash flow after another, ever freeing him or herself to undertake new projects.

Perhaps it shouldn't be surprising, then, if we discover that traits associated with leadership are also desirable in the founders of new firms. Fairly consistent findings in the literature on the funding of new technology-based ventures support this supposition. We have recently found that empirical works on leadership from the resourcefulness perspective may contribute to a better understanding of some key criteria used by venture capital firms to screen new ventures.

The Decision Criteria of Venture Capitalists

Most of the research on the venture capitalists' investment criteria have found that the investors' decision-making process is embedded in multi-staged activities during the pre-investment period. The deal originating stage, which is the first step, consists of the identification of potential investment prospects. Since most of the latter are too small to be easily identified, venture capitalists often have recourse to either personal or professional intermediaries. As venture capital firms generally specialize by geographic region, industry, size of investment, and stage of investment, the second stage, deal screening, consists of selecting out prospects which do not belong to the investors' areas of specialization. At the third stage, deal evaluation, each venture is assessed on multidimensional characteristics including financial and marketing projections. Investigation may be undertaken to insure the

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accuracy of the information provided in the business plan its founders submitted. The last stage of the pre-investment period consists of the structuring of a mutually acceptable agreement between the venture capitalists and the entrepreneurs and which comprises a specification of the equity share the founders are willing to give up in exchange for the venture capital.

MacMillan et al. (1985) provides a basis for subsequent works (see Table 1) on the venture capitalists' decision-making process. The authors identified four main groups of criteria used by investors when evaluating prospects -either with an eye to selection, or with an eye to predicting project performance. Marketing-related criteria are those used to assess the growth potential of the market targeted by the venture. Finance-related criteria include most importantly the expected rate of the return and the cash-out potential. Product/technology-related criteria are used to assess the superiority of the product or concept and its degree of innovativeness. Management-related criteria includes principally the personality, experience and capabilities of the entrepreneurs.

Table 1 The Decision Criteria of Venture Capitalists

Common to these studies on the key criteria used to screen technology-based ventures (MacMillan et al. (1987), Hall & Hofer (1993), Knight (1994), Guild & Bachher (1996), Bachher (1999)) was the conclusion that the management-related-criteria are considered by venture capitalists the factors which most influence their decision-making. The quality of the entrepreneurial team is the principle reason for awarding funding. Investors prefer a mediocre project led by a very good team to an excellent project led by mediocre entrepreneurs. Many groups of sub-criteria are comprised in the management-related category as shown in Table 2.

Table 2 : management-related criteria used by venture capitalists to evaluate new ventures

Specific Skills	Marketing, communication, technology-related
Experience	References, familiarity with the market, leadership ability demonstrated, relevant track record, familiarity with team's reputation
Commitment to the new venture	Sustained and intense effort, commitment to success
Compatibility with the venture capitalist	
Ability to build team	Ability to recruit, ability to create high standards of team performance
Ability to focus on results	Ability to anticipate problems, ability to encourage team to be result-oriented
Understanding of the market	
Ability to execute on strategy	Ability to follow on through a strategy, ability to create value for future shareholders

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Ability to manage change

Ability to anticipate need for change, ability to accept a change in roles, ability to bring about change, ability to effectively manage change, ability to be flexible with the venture's strategy

Managerial capabilities and business awareness

Familiarity with technology enablers, ability to evaluate and react to risk well, ability to articulate well when discussing venture, attention to details

Sources : MacMillan et al. (1985), Guild & Bachher (1996) and Bachher (2000).

Although elements belonging to the management-related category of criteria have been clearly identified, they remain very difficult to measure and are subject to bias as their assessment is subjective. As regards quality of the entrepreneurial team, venture capitalists' decision process lack objectivity and entrepreneurs still remain in the dark. In consequence, mediocre projects may be funded, and good projects may never get the financing they need. Without sufficient financing, good projects may either reach an demise or move abroad, thus not contribute to the growth of their local economy. There is a need for more systematic methods of evaluating the quality of management and the entrepreneurial team.

An Overview of the Research on Leadership Traits

There is a vast literature on the traits characteristic of leaders, and Kanungo and Misra (1992) provide an effort to synthesize this research. These authors emphasized the importance of competencies versus skills as regards managerial capabilities. They were able to summarize all previous empirical research on leadership traits by grouping the traits in three categories of competence , namely affective competence, intellectual competence and action-oriented competence, as components of managerial resourcefulness. A resourceful leader/manager is thus an individual who shows competence in self-regulating his or her emotions/feelings, thoughts and actions while performing managerial roles or executing managerial functions, though faced with unstructured, discretionary, non-routine and non-specific tasks. Table 5 presents the three categories of competencies related to resourcefulness as conceptualized by Kanungo and Misra (1992) and the corresponding categories of leaders' qualities Kanungo and Menon (1996) found in their empirical work when they operationalized resourcefulness.

Through a survey of 485 managers, Kanungo and Menon (1996) identified items (either descriptive of a behaviour or indicative of a preference) which were best related to competencies of resourceful managers. They classified these items into four generic competencies. Emotional equanimity (EE), which corresponds to affective competence in the Kanungo & Misra conceptualization, includes such items as control of strong primitive reactions and anxiety.

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Table 3: Conceptualization and operationalization of resourcefulness

Resourceful leaders/managers' qualities (Kanungo & Menon, 1996)	Managerial competencies as components of resourcefulness (Kanungo & Misra, 1992)
Emotional equanimity (EE)	<p>Affective competence</p> <ol style="list-style-type: none"> 1) Control of primitive reactions in situations that produce strong emotions 2) Development of equanimity and problem orientation 3) Delay of gratification 4) High proactive involvement, enthusiasm, interest and commitment to meeting challenges in life
Proactive analytical orientation (PAO)	<p>Intellectual competence</p> <ol style="list-style-type: none"> 1) Competence to solve problems 2) Self-reflection for strengthening self-efficacy belief
Problem-focused perseverance (PFP)	<p>Action-oriented competence (task-oriented)</p> <ol style="list-style-type: none"> 1) Attention to details 2) Persistence to pursuits 3) Concern for time frame.
Goal directed problem orientation (DGPO)	

Proactive analytical orientation (PAO) , which best corresponds to intellectual competence, includes behaviours and preferences epitomizing the use of planning deliberations, goal component analysis and diagnostic information generation to understand and solve problems. Problem-focused perseverance (PFP) , which corresponds to action-oriented competence, is comprised of items indicating persistence in task pursuits and care for details. Goal directed problem orientation (GDPO) constitutes a fourth generic competence and is an overarching category consisting of the ability to keep thinking, feeling and action oriented towards the pursuit of the goal. This study also found a strong and positive correlation between those items related to resourcefulness and those related to self-efficacy belief and empowerment. Using another independent variable which is associated with managerial success, managers' salary, this study found that resourcefulness is highly and positively correlated to success. The researchers concluded and suggested that such a psychometric and sound measure of

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managerial competencies be used in selection and training of managers and leaders.

The preferred entrepreneurs - the resourceful leaders : how do they compare?

Table 4 : Resourcefulness and managerial capabilities

Venture team characteristics	Resourceful leaders characteristics
Commitment to the new venture	DGPO, PFP
Compatibility with the venture capitalist	GDPO, EE
Ability to build team	PAO, EE
Ability to focus on results	GDPO, PAO, PFP
Ability to execute on strategy	GDPO, PAO, PFP
Ability to manage change	PFP, PAO
Managerial capabilities and business awareness	GDPO, PAO, EE

Specific skills and past experience as sub-criteria to managerial characteristics in the venture selection process are easy to assess because they are skill-related. However, all the other items need sound and objective measures, since they are more competence-related. In opposition to skills, competencies are transferable because they are generic in nature, used to handle non-routine tasks and dynamic environments, and are person-dependent. Comparing the behaviours and preferences found in resourceful leaders to the preferred characteristics of venture team in venture capitalists' investment decision-making, we found that many of the latter require emotional equanimity, problem-focused perseverance, proactive analytical orientation and goal directed problem orientation (see table 3) and thus affective, intellectual and action-oriented competencies.

Conclusion

This observed correspondence between leadership traits and the required characteristics of new venture founders entails research implications for both the field of venture capital decision-making and that of leadership.

For the MacMillan vein of research which found the management-related criteria as the most important factors in venture capitalists' decision making, empirical studies may be undertaken to discover whether there is indeed a high and positive correlation between the items related to resourcefulness and those associated with the investors' preferred entrepreneurs, and whether having traits and competencies of resourceful leaders may effectively help entrepreneurs be successful in their fund seeking process.

The research on leadership traits may find a new field for studying these traits.

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As for practice, principles of new ventures selecting candidates for their entrepreneurial team may use resourcefulness, as operationalized by Kanungo and Menon's work, as a selection and training tool. Similarly, this instrument may help venture capitalists rethink their selection criteria and establish more reliable and objective measures, thereby promoting transparency in the venture capital marketplace..

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