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# Venture capital in Latvia: the peculiarities, contradictions, and accessibility for SMEs

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## Abstract

The authors of this article pay particular attention to the study of the nature of venture capital as a multi-meaning concept. It is evident that venture capital is one of the main sources of financing innovation entrepreneurship and small business. On the other hand venture capital represents an independent sector of market economy of a certain country. At the same time venture capital operation mechanism requires a definite system of public relations in risky business, which is based on economic interests of investors, entrepreneurs, government and society. The *purpose* of this research is, on the basis of the investigation, analysis and synthesis of contemporary publications on the topic of venture capital and opinions of Latvian venture investors, to make an attempt to evaluate the role of venture capital in the development of entrepreneurship and small businesses in Latvia, identifying the peculiarities and contradictions of its functioning in the conditions of entrepreneurial environment in the context of globalization.

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*Keywords:* venture capital, investors, venture capital funds, small business financing

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## 1. Introduction

Despite the fact that in Latvia the number of publications and research papers on the topic of venture capital investments has increased over the last years, the phenomenon of venture capital and its operation mechanism have not been sufficiently scrutinized yet. The European Venture Capital Association

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(EVCA) keeps records only of the whole Baltic region. It is understandable as most of the funds focus their investments on all three Baltic countries or even more widely on the CEE and Russian region according to the research “Venture capital in Latvia revisited”. According to this study, in 2007-2008 venture capital investments in Latvia accounted for only 0.29% of GDP, whereas venture capital investments per capita were 30 euro (Vanags, Staševska and Paalzow, 2011). The data that has been presented by the Latvian researchers from Stockholm School of Economics in Riga shows that total amount of venture capital invested in Latvia equal to 215.2 mEur (Krits, Strenga, and Paalzow, 2013). Venture capital as a research object has been receiving increasing attention from modern scientists, academics, and practitioners. This phenomenon is multifaceted and unique. On the one hand, it represents the type of economic activity, which embodies intellectual entrepreneurship; on the other hand, it is one of investment forms characterised by high risk and high return on investment. In addition, during the venture capital investment implementation process a certain system of relations occurs, which involves investors, entrepreneurs, managers, society and state. Therefore a study of the peculiarities of this system operation as the factor that determines the success of venture capital investments may also become an independent piece of research.

There are also practical aspects that enhance the relevance of the topic. Many Latvian investors, who call themselves venture investors, are complaining about the lack of interesting innovative projects and point out the inertia among Latvian entrepreneurs. At the same time, entrepreneurs, who have unconventional innovative ideas, are complaining that they cannot get through to venture capitalists. It is clear that Latvia has not yet developed a system of effective venture capital investment; and this area of research remains a topic for debate and discussions. The result of this paper is a list of recommendations aimed at creating an effective mechanism for the venture capital investment operation as a vital funding source for innovative SMEs in Latvia. These recommendations are primarily designed for public institutions, as the authors attach critical importance to the position of the state in this matter.

## 2. Literature Review

Peculiarities of venture capital in Latvia were studied by Lace and Laizans (2007), the problems of management innovation activity were outlined by Denins and Zakovics (2008); Kopitov (2004) explored the possibilities of attracting venture capital to the transport sector; innovative business financing questions were presented in the paper by Jakusonoka and Prohorovs (2011); the impact of corporate tax on innovations was researched by Zelgalvis and Joppe (2011). An attempt to examine the size and scope of the venture capital sector in Latvia was undertaken by Vanags, Staševska, and Paalzow in “Venture Capital in Latvia Revisited” (2010). In order to draw attention to the venture capital industry, some venture capitalists publish their own materials in the Internet (Tamuzs V., Sosars V., Riksis M., Prohorovs A., and Berzins A. working most actively in this field). In general terms the mechanism of venture financing is presented by the Directorate of the European Commission in the form of “The Guide to Risk Capital Financing in Regional Policy” (2004) and is available in the Internet.

Venture capital definitions offered by a number of venture capital associations and some researchers are provided below. Venture capital is: *Long-term investment* in the company’s equity with the purpose to promote the value of the company by financing its rapid growth and development (LVCA); *Subset of private equity* which is broadly defined as the provision of equity-oriented financing to enterprises that are not listed on a stock market (EVCA); *Specific type of finance* well suited to the requirements of new

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