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EQUITY BUILDING ACTIONS OF NEW VENTURES IN A HIGH-VELOCITY MARKET: RESEARCH ON TAIWAN' S INTERNET ENTREPRENEURIAL ORGANIZATIONS

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ABSTRACT

Based on the theories, such as the resources-based theory, new product development and strategic alliances, we proposed the equity-building actions of new ventures in the Internet industry. We note that the new ventures' purpose in capital raising actions before going public is not simply to raise funds, but to obtain rare resources and build core competence through equity invested or conjoined. Through interviews, we discuss factors that affect the equity-building process, and propose two propositions. Firstly, the original core resources of new ventures will affect the equity-building process. Especially, on target selecting, alliance timing, and alliance preference. Secondly, equity-building actions before IPO are parts of a growing strategy for emerging firms. The findings of this research are helpful in understanding the linkage between resource endowment and equity-building actions, and for new ventures to build up competitive advantages during founding period.

Keywords: Equity building, Resource-based Theory, Internet Ventures, Strategic Alliances

INTRODUCTION

In the last year the Internet business has been booming and faced rapid recession. The rapid growth of companies such as Amazon, Yahoo, American Online has overturned many traditional business models and paradigms, and their founding processes have attracted many discussions. In the case of SINA.com, its plural shareholders include Dell Computer Corp., Goldman SachsGroup Inc., Softbank Corp., Sumitomo Corp., Pacific Convergence Group, Trend Micro Corp., and United Overseas Bank of Singapore et al. All these different investors, including venture capital, intermediary financial institutions or related industry firms, aim to infuse huge amounts of financial capital into a new Internet venture where its product is not mature or it cannot break-even. From the standpoint of the new Internet venture, is there any criterion for cooperation partners and the sequence? Can a new venture located in a high-velocity market shorten the time to gain resources, or integrate the capital-raising purpose with future development through an alliance? From the resource-based view, the new venture can gain necessary resources through an alliance and shorten the resource-searching time by cooperation with resource-matching partners [13][22]. It suggests a possibility that the characteristics of a new venture's resource endowment may influence the alliance preference and alliance partner decisions. So this is influential in the equity-building action, i.e., major behavior in the alliance.

In order to realize the causality of the equity-building actions of new Internet ventures, this research focuses on how the owned resource characteristics of a new Internet venture are influential in equity-building motivation and sequence. Through interviews with several Internet ventures, we try to realize the relationship between owned resource characteristics, alliance preference in different growth stage, and try to find the possible alliance mechanism for new Internet ventures. The next sections are related literature review, research methods, results and discussions.

LITERATURE REVIEW

In the financial field, equity building is a part of the financial decision for firms. However, from the financial viewpoint, there are some restrictive assumptions, such as open capital market condition, which is not suitable for the new ventures' equity raising channel. For new ventures located in a highly changeable market, their equity building actions may contain several motivations. It is not just for raising sufficient financial capital, but also for growth, maximizing value, developing new products and searching for competitive advantage et al [13]. In order to achieve these different motivations, new ventures must realize their own resource set, how their resources are helpful for these motivations, and try to shorten the time for achieving aims by cooperating with others. It suggests that the resource-based theory which explains how resources could be the origin of competitive advantage, and the strategic alliance which focuses on the inter-firm cooperative behavior would be suitable ways of understanding equity building actions of new ventures. Next, we review the related literatures.

Rationalizing Capital Raising from Resource-based View

For realizing the raising capital subjects of new ventures, researchers have been explaining the relationship between different development status and suitable financial objects [4]. They suggest that in the initial founding stage, for a lack of guarantees and transaction records, it is better to finance from entrepreneurial groups, family or friends. However, they don't explain satisfactorily the reason for financial sequence and criterion in choosing finance objects. Also, they suppose the relationship between different finance and development status occurs in a straight-line. This opinion cannot adequately explain the real relationship between finance and development.

For a new venture located in a highly uncertain environment, it must gain the necessary capital and resource as soon as it can. In this situation, the equity building actions may relate tightly with its future development, and the equity-building process will not absolutely follow the route suggested by Berger and Udell [4]. When considering the entrepreneur's strategic purpose, such as a growth or technological application strategy et al., in the founding process, it is suitable from the knowledge-based opinion to say that the entrepreneur's strategic purpose could be the criterion as to where this new venture will have enough resources or not [6][15]. The origin of the knowledge-based opinion is resource-based theory [6].

From resource-based theory, a firm is a set of resources it owns. The main concern for resource-based theory is how the firm can utilize its resources to achieve sustainable competitive advantage [3][31]. The resources for achieving competitive advantage have value, scarcity, imperfect imitation, and imperfect substitution characteristics [3][24]. The resources characterized above will let the firm sustain some degree of heterogeneity [24]. In the resource-based view, "a firm's competitive position is defined by a bundle of unique resources and relationships" [27, p.557].

However, the resource-based view has been criticized for not adequately explaining how and why certain firms have competitive advantage in situations of rapid and unpredictable change [29]. In the market characterized by vague boundaries and where the business model is not clear, a firm must utilize 'dynamic capabilities'. This is defined as 'the firm's ability to integrate, build, and reconfigure internal and external competences to address rapidly changing environments' [29, p.516] to achieve competitive advantage. Dynamic capabilities are a set of identifiable and specific processes such as product development, strategic decision-making, and alliances [12]. In high-velocity markets such as the Internet market, dynamic capabilities are simple and experiential routines that rely on newly created knowledge specific to the situation [12]. The targets of dynamic capabilities are for firms to gain the necessary resources, and then achieve competitive advantages. How does a firm form dynamic capabilities and gain the necessary resources in a high velocity environment? The alliance method is feasible.

Resources types, Strategic Alliances and Equity-building Sequence

In order to react to the high velocity market as soon as possible, a new venture in this market must form dynamic capabilities, and shorten the forming time. When a firm lacks necessary resources, which may be characterized as imperfectly movable [9], lacking transparency [19], tacit, complex and specific [26], or imperfectly imitated or imperfectly substitutive [3][24][31], then it must search for these resources outside. This searching process is a kind of dynamic capabilities. One of the most frequently used resource-search methods is the strategic alliance. The alliance motivations from resource-based view are obtaining the partner's resources and retaining and developing one's own resources by combining with the partner's resources [8]. From the resource-based view, the definition of strategic alliances is 'cooperative relationships driven by a logic of strategic resource needs and social resource opportunities' [13, p.137]. If the strategic alliance is for developing a new product, then this is defined as a 'new product development alliance' [22], and it means any formal and informal contracts related with developing and commercializing new products.

The resource-based view of explaining alliances combines the different needs for alliances suggested earlier, i.e., the strategic needs (e.g., [2][23]) and the social opportunities (e.g., [17][25]). Alliances form either when firms are in valuable strategic positions for which they need additional resources that alliances can provide, or when firms are in strong social positions such that they have the resources necessary to know, attract, and engage partners [13, p.138]. Das and Teng [7] suggest that the relationship in strategic alliances can be categorized by the partner's intention of resource and risk. They suggest [8] that the two sides' resource characteristics are related with the typology and preferred structure of the strategic alliance.

Of the several categorizations for resources, such as tangible and intangible resources [16], physical, human and organizational capital resources [3], namely, financial, physical, technological and managerial resources [7], or properties-based knowledge-based resources [20] et al., each has its limitation and particular background. In discussing the alliance relations for new Internet ventures, categorization by property, such as human or physical, or by usefulness, such as namely or managerial resources is insufficient. For the former, one indicated property of resources may have several applications in an enterprise, or may have a different application in another enterprise. It means that this categorization by property has its limitations. For the latter, the indication of resources to a specific use is unclear and may lack paradigms for the Internet business. We use the categorization suggested by Miller and Shamsie [20] to avoid the possible mistakes above. This categorization can label the nature of resources for the Internet business.

According to the related research [8][20], resources can be categorized as property-based or knowledge-based. For the former, it is legally defined as the property owned by a specific company such as financial capital, real assets, patent, brand and human resources et al. The owner has clear ownership and can dispose of these resources. There are differences in property-based resources, for example, the human resource is imperfectly movable, patent and brand are imperfectly imitative, and the real assets are imperfectly substitutive. For the latter, it is related to intangible assets such as management capability, knowledge and technology. Because knowledge-based resources are characterized as imperfectly movable, and it exits causal ambiguity between these resources and competitive advantages, they are difficult to imitate by other competitors. However, under specific conditions, some kinds of knowledge-based resources are movable, such as patent technology trading, or head hunting. When discussing the motivations for an alliance, it is necessary to consider property-based and knowledge-based resources simultaneously. Because lacking the legal protection, all kinds of resources can be imitated or duplicated during trade. Then the firm would lose any motivation to trade or form alliances.

The opinion suggested by Das and Teng [8] that the resources type, i.e., knowledge-based or property-based type, influences the alliance structure is insightful in analyzing the alliance motivation and criterion of new Internet firms. However, Internet firms may form several alliances at the same time. Alternatively, it may intend several motivations with one alliance partner. It is difficult to distinguish the real relationship between a specific alliance structure and the resource type. The steps described in 'new product development alliance' [22], which include awareness, exploration, commitment and dissolution can be implemented in analyzing the collaboration and development process of new start-up Internet firms. This concept suggests the possible process of Internet firms' collaboration, such as contracts of co-development of the new product, sales contract, marketing contract and equity coalition. No matter what the alliance motivation is for developing a new product, such as a gain in the partner's reputation [28], the new Internet firm forms alliances according to its core resource type and growth strategy. We propose that the new Internet firm uses alliances to gather necessary resources for development, its core resource type is influential in searching for an alliance partner with resource-matching characteristics, and its alliance partner and sequence is related tightly with its growth stages.

Summary

Using the resource-based theory and strategic alliance opinion, we try to analyze the equity building motivation and process for new Internet firms. For a new Internet firm located in a rapidly changing environment, it can enhance its new product development ability [22] and gain necessary resources [13] through alliances. It may look for a suitable partner by following a particular rule. This rule is for the purpose of searching for a resource-matching partner in a different growth stage. We attempt to confirm these opinions.

RESEARCH METHODS

Using an interview method, we try to understand the equity building process of new ventures. There are four criterions for screening suitable firms, including: (1) Internet company: where above 40% of revenue in this company comes from Internet related industries; (2) new venture: this company is founded after 1994; (3) public offering company: this company need not to be a listed company, but it must have diverse stocks and have contact to the open capital market; and (4) restriction on shareholder structure: the company cannot be a family business, spin off company or non-legal person business. After screening and contact with 23 possible firms, 6 firms agreed to accept an interview, 3 firms agreed to fill in the questionnaire. Of these 9 questionnaires, 1 is invalid. So we gathered 8 cases at all. The interview questionnaire is a semi-structured questionnaire, and the interviewee is restricted on the general manager or other top managers who are familiar with the founding process. Besides the interview questionnaire, we refer to the secondary data to complement the target firm's background.

The questionnaire design contains four parts. One is the basic founding period description, including founding time, founding capital size, and initial founding product et al. We still survey the core resources or capabilities in the founding period. The other three parts are designed for realizing the firm's resources from partners and resource providers at different capital raising stage. We categorize the firm's core resources and resources from partners into property-based and knowledge-based resource groups. In the categorization of the 8 firms, they are judged according to their own founding product, core founding resource and main revenue origin (see Table 1). In the resources from partners, all the possible resources items are listed for convenience, i.e., technology, management capabilities, sales channel, reputation, network relationship, marketing and sales assistant, product manufacturing capabilities and etc[i]. In order to understand the partner's characteristics, we categorize partners into 9 types, i.e., friends and family, private investor, venture capital, government, financial intermediaries (banks, security corporations et al.), breeding incubator, related industrial firms, business group and others. Through the responses by the interviewee, we analyze the relationship between the firm's core resource type and

Table 1: Firms Categorization According to Resource Types

	Answer Online, Inc.	Dreamer's Media Inc.	Money DJ, Inc.	Jade Pacific Corporation	Cityfamily Online, Inc.	Ecom Software Inc.	Formosoft Internation Inc.	Tornado Tech Inc.
Founding Product	Virtual Channel and Website	Portal	Online Stock Database	Internet Application Software	Internet Software	Internet Application Software	Internet Application Software	Internet Application Software
Founding Resources	Business Idea Innovation	Business Idea Innovation	Business Idea Innovation	Business Idea Innovation	Technology (Including Patents)	Industry Management Capabilities	Technology	Technology (Including Patents)
Main Revenue Origin	*Mobile Phone *Mobile Phone Number *Fittings	*Advertise *Homepage Design	*Financial Information Integrated System *Service Electronic Commerce	*Financial Information *Electronic Commerce	*Internet Advertise Database *Website Building *Electronic Commerce	*Internet Management Application Software *Software Leasing Service	*Visual Software *Word Discriminating Software *Internet Application Software	*Knowledge Service Platform *Virtual Community Platform
Core Resource Type	Knowledge-based	Knowledge-based	Knowledge-based	Knowledge-based	Property-based	Property-based	Property-based	Property-based

resources from the partner. We then rationalize the relationship and sequence between resources from partners and alliance partners at different growth stages. For lack of cases, all the possible results are analyzed qualitatively.

RESULTS

According to the literature, we suppose that the motivation in different capital raising stages and proposed partner are different for firm with different resource types because its resource characteristics and resource needs are different. The different motivation may reveal the sequence of choosing the alliance partner and alliance preference. We describe and compare the difference between the two types of firms, and later derive related propositions.

Core Resources Type and Alliance Sequence

In the resource-based view, the firm's core resource characteristics would influence the alliance type and preferred partners at different developmental stages. From the interview, we observe that the firms with same resource types reveal a similar preference in alliance partners and sequence. For the knowledge-based firms (see Table 2), all choose to initially raise capital from friends and family or private investors in order to avoid possible resource exploitation by partners. They would initially choose partners for pure financial support, and build equity relations with other knowledge-based firms after the barrier of transferring its core resources is higher or when its product development stage is more mature, i.e., after stage C.

Property-based firms (see Table 3) build external equity relations in the initial stage, and at an immature product development stage (before stage C). Their main equity-building partners include venture capital and related industry firms. Compared with knowledge-based firms, property-based firms utilize external equity relations relatively early and they have a deeper interaction with partners. For the firm whose core resources are of a property-based type, it is convenient for this firm to control the transference and utilization of resources. It would enter into the tighter equity-building relations in order to gain the required resources from partners, and especially cooperate with firms with knowledge-based resources.

Analyzed above, the core resource type would influence the alliance preference and partners. Then, we propose the first proposition.

Proposition 1: The Internet new venture's core resources type would influence its alliance preference and sequence.

Proposition 1-1: If a firm's core resources are knowledge-based, its purpose in equity-building is to protect its resources and not be exploited or imitated by partners. Therefore, this kind of firm would choose partners who provide pure financial resources in the founding period and

Table 2: The Equity Building Behavior for Knowledge-based Firms

CAPITAL RAISING STAGE	ANSWER ONLINE, INC.	DREAMER'S MEDIA INC.	MONEY DJ, INC.	JADE PACIFIC CORPORATION
Founding Capital Raising Product Development Stage	Friends and Family (Internal Finance) Stage A	Friends and Family Private Investor (Internal Finance) Stage A	Friends and Family (Internal Finance) Stage A	Friends and Family (Internal Finance) Stage A
First capital Raising Stage Product Development Stage	Friends and Family (Internal Finance) Stage C	Employee, Initial Shareholders (Internal Finance) Stage D	Employees (Internal Finance) Stage C	Employee, Initial Shareholders (Internal Finance) Stage C
Second Capital Raising Stage Product Development Stage	Private Investor, Initial Shareholders (Internal Finance) Stage D	Initial Shareholders (Internal Finance) Venture Capital (Knowledge-based) Stage E	Employees (Internal Finance) Stage D	Private Investor, Initial Shareholders (Internal Finance) Stage D
Third Capital Raising Stage Product Development Stage	Initial Shareholders (Internal Finance) Stage D	Venture Capital (Knowledge-based Stage E	Initial Shareholders, Private Investors (Internal Finance) Venture Capital (Knowledge-based) Stage D	Initial Shareholders (Internal Finance) Venture Capital (Knowledge-based) Stage E
Forth Capital Raising Stage Product Development Stage	Related Industry Firms Venture Capital (Knowledge-based) Stage D	Financial Intermediaries (Knowledge-based) Stage E		Venture Capital (Knowledge-based) Stage E
Fifth Capital Raising Stage Product Development Stage	Related Industry Firms (Property-based) Venture Capital (Knowledge-based) Stage E			

P.S.: The definition of each product development stage is listed:

(1) Stage A: The firm just has concept for product, not researches and develops completely;

(2) Stage B: The R&D for product is completed, but not commercialized;

(3) Stage C: The firm is going to promote the commercialized product;

(4) Stage D: The product goes on the market, and on marketing;

(5) Stage E: The product goes on the market, and is well known by customers.

build external equity relations after its product is mature.

Proposition 1-2: If a firm's core resources are property-based, its purpose in equity-building is to gain necessary resources through alliances. Therefore, this kind of firm would choose plural alliance partners in the founding period, and build external equity relations early.

Environmental characteristics and Alliance Purpose

The firm's core resource type would influence the alliance preference, and the firm's environment would influence the alliance purpose. An Internet firm located in a high velocity environment must shorten the searching and forming resource time as much as possible. In order to gather the resources necessary for growth, the firm needs to cooperate with others. The alliance purpose is not solely for raising financial capital. Through interviews, we observe that the firm's equity-building motivation at different developmental stages is tightly related with its growth or product development. The firms whose core resources are knowledge-based, i.e., Answer Online, Inc., Dreamer's Media Inc., Money DJ, Inc. and Jade Pacific Corporation, and the firms whose core resources are property-based, i.e., CityFamily Online, Inc., Ecom Software Inc. and Formosoft Internation Inc., are motivated to build equity actions not only for the purpose of raising financial capital (for details, see Table 4). There are

Table 3: The Equity Building Behavior for Property-based Firms

CAPITAL RAISING STAGE	CITYFAMILY ONLINE, INC.	ECOM SOFTWARE INC.	FORMOSOFT INTERNATION INC.	TORNADO TECH INC.
Founding Capital Raising Product Development Stage	Friends and Family (Internal Finance) Stage C	Related Industry Firms (Knowledge-based) Venture Capital (Knowledge-based) Private Investor Stage B	Employee, Initial Shareholders (Internal Finance) Venture Capital (Knowledge-based) Stage B	Venture Capital (Knowledge-based) Business Group (Knowledge-based) Stage D
First Capital Raising Stage Product Development Stage	Initial Shareholders (Internal Finance) Stage D	Employee (Internal Finance) Stage D	Employee, Initial Shareholders (Internal Finance) Stage D	Initial Shareholders (Internal Finance) Stage D
Second Capital Raising Stage Product Development Stage	Employee, Initial Shareholders (Internal Finance) Related Industry Firms (Knowledge-based) Stage E	Related Industry Firms (Knowledge-based) Venture Capital (Knowledge-based) Business Group (Knowledge-based) Stage D	Initial Shareholders Private Investors (Internal Finance) Venture Capital (Property-based) Stage D	Initial Shareholders (Internal Finance) Venture Capital (Property-based) Stage E
Third Stage capital Raising Product Development Stage	Initial Shareholders Private Investors (Internal Finance) Related Industry Firms (Knowledge-based) Venture Capital (Knowledge-based) Stage E			

P.S.: The definition of each product development stage is same as Table 2.

Table 4: The Equity-building Motivations Listed

	ANSWER ONLINE, INC.	DREAMER'S MEDIA INC.	MONEY DJ, INC.	JADE PACIFIC CORPORATION	CITYFAMILY ONLINE, INC.	ECOM SOFTWARE INC.	FORMOSOFT INTERNATION INC.
Founding Capital Raising	Financial Capital	Financial Capital	Critical Management Resources	Financial Capital	Financial Capital Critical Management Resources	Financial Capital	Critical Management Resources
First Capital Raising Stage	Financial Capital	Others: Creating Corporation Values	Others: Attracting Talented Workers	Financial Capital	Legitimization and Reputation	Others: Attracting Talented Workers	Critical Management Resources
Second Capital Raising Stage	Financial Capital	Reputation Others: Institutionalize Firm's Process	Others: Attracting Talented Workers	Financial Capital	Building Management Networks	Others: Increasing Size	Financial Capital
Third Capital Raising Stage	Financial Capital	Others: International Resources	Financial Capital	Legitimization and Reputation			
Forth Capital Raising Stage	Legitimization and Reputation	Others: IPO Projects		Legitimization and Reputation Building Management Networks			
Fifth Capital Raising Stage	Others: Increasing Size						

P.S.: We exclude the Tornado Tech Inc. in this part for its answer is invalid.

motivations other than the firm's growth or product development. All the interviewees mention the importance of alliances at different developmental stages, and all agree that the purpose for alliances is not just for raising financial capital. The alliance must relate tightly with the firm's growth and future strategic intentions. It means that equity-building actions of Internet ventures cannot be solely explained from a financial point of view. The related proposition follows.

Proposition 2: When the located market environment is of a high velocity type, the firm would choose the partners matching its growth in the founding period. In other words, the equity-building actions of new Internet ventures are a part of their growth strategies.

CONCLUSIONS AND DISCUSSIONS

From the opinions of resource-based theory, new product development and strategic alliance, we try to explain the equity-building action, motivation and process of new Internet firms. Using an interview method, we find that the equity-building actions of new Internet firm are tightly related with its growth and future development, and the core resource type is influential in deciding the firm's alliance partners and sequence. For firms with different core resource types, i.e., knowledge-based or property-based type, there can be different equity-building actions and preferences. The firms with knowledge-based resources, i.e., Answer Online, Inc., Dreamer's Media Inc., Money DJ, Inc. and Jade Pacific Corporation, are more conservative in developing equity-building actions outside than firms with property-based resources, i.e., CityFamily Online, Inc., Ecom Software Inc., Formosoft Internation Inc. and Tornado Tech Inc. The former prefers to cooperate with familiar personnel networks, such as friends, family or private investor in founding period, and the latter prefers to build equity relations with whom they can provide managerial capabilities, such as related industry firms, venture capital, et al. in founding period. The resource type may not only influence the alliance partner, it can also influence the alliance sequence that is closely related with the firm's growth or strategic development. These findings are important in realizing the relationship between capital raising and growth in the founding period of the Internet business. Also, they may provide concrete helpfulness when considering the preferred equity-building sequence and partners.

The resources owned by a firm really matter. In the founding period, the resources are crucial in deciding the equity-building actions, and are closely related with future development. However, there are some limitations in this research. Firstly, lacking sufficient cases, we can only confirm the proposed opinions using the qualitative interview method. Future quantitative research would be helpful in understanding the mechanism of resource types and equity choice. Secondly, the informer's cognition and personal judgment may create inaccuracies cannot be avoided. The Internet business has changed rapidly in the last year. It deserves further research in order to understand the Internet firms' behavior in the founding period, and provide feasible business development suggestions for this industry.

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[i] In the categorization of resources from partners, we separate these resources as: (1) knowledge-based resources: technology, management capabilities, network relationship, marketing and sales assistant and product manufacturing capabilities; (2) Property-based resources: technology, sales channel, reputation and product manufacturing capabilities.