



# The Trend of Venture Capital and Its Contribution to The Country and Enterprises A Case Study of Venture Capital in China

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## ABSTRACT

In recent years, venture capital is booming all over the world. Its development has changed from localization to globalization, from developed countries gradually extended to developing countries. Its remarkable returns and star cases have made people salivate. At the same time, the government is also supporting the development of venture capital because of its promoting effect on society and enterprises. With the boom of the Internet, more and more people realize the benefits of venture capital and try to enter the industry. However, they ignore the failure rate of venture capital. This paper will start from the case of venture capital in China, analyze the development trend of venture capital and listed enterprises, and explain its benefits to the country and enterprises. Also, this paper will point out the problems that venture capital may face, and give the possible development direction of venture capital in the future, so that investors can make decisions and improve their success rate.

**Keywords:** *Venture capital investment trends, the role of venture capital, listed companies*

## 1. INTRODUCTION

In recent years, venture capital has become more and more prosperous around the world. With the boom of the Internet, more and more successful cases have been spread around the world, and the super-high rate of return of venture capital has gradually shown in front of people. With the development of globalization, people are increasingly aware of the opportunities emerging in developing countries, and venture capital is also becoming globalized. At the same time, the benefits of venture capital for the country and enterprises have gradually been discovered by more people, and the government has begun to encourage the development of venture capital. In this wave, countless people go to the field, trying to get a chance to get rich overnight, but they also ignore the extremely high failure rate in this field. This paper will start with the situation of Venture capital in China and analyze the benefits of venture capital for the country and its enterprises. And summarize the trend of venture capital investment, so that investors can make a better judgment based on the data, improve the success rate of investors and point out the direction of the next possible evolution of venture capital.

## 2. LITERATURE REVIEW

Sahu et al. researched private equity and venture capital trends in recent years. Private equity has expanded into more areas in recent years, helping companies create value while making big profits through efficient exits. Also, venture capital tends to invest in developing countries and emerging areas, but it is increasingly constrained in developing countries [1]. Wong and Anson's research has shown that venture capital has boomed in China over the past three decades. In the beginning, it was led by foreign institutions and gradually became the joint efforts of foreign and domestic institutions. At the same time, investment is shifting from information technology to financial services. Also, the type of VC investment mostly ventures capital (59%) [2]. Kochura's research shows that venture capital plays a positive role in financing knowledge-intensive enterprises. Venture capital also makes effort in promoting the stock market, retaining high-quality talents, and developing science and technology. Moreover, it helped the country and mankind become better [3].

Tohmatsu finds that nowadays people live in a globalized world, and venture capital is gradually

expanding from local investment to global investment, to adapt to the tide of globalization and get more lucrative profits [4]. Caselli and Negri researched that the relationship between private equity and venture capital is more of a condescension. According to the research, venture capital is more inclined to enter early, while private equity is more like an investment behavior after the company matures. Private equity helps venture capital to obtain excess returns while also helping themselves to grab the profits of the company's sustainable development [5].

Cochrane researched that venture capital bears high risks as well as high returns, but its risks are acceptable and cover the demand for returns [6]. Through Sahlman's research. It is found that the original capital of venture capital mostly comes from individuals and organizations, and its investment preference is mostly high-risk and high potential early enterprises. The internal organizational structure of venture capital is rigorous and complex to achieve the purpose of high efficiency and high returns [7]. From the research written by Gompers, it is found that with the difficulty of venture capital investment increases, venture capital is more inclined to invest money in early high-tech companies, and venture capital use the information gap to analyze the situation of investable enterprises. Moreover, the venture capital is no longer a constant investment. After continuous tracking and detailed analysis of the company's situation, venture capital will selectively continue some projects and terminate other projects [8].

Kaplan and Stromberg researched that the significant characteristic of venture capital financing is that the venture capital capitalists are allowed to allocate cash flow rights, board rights, voting rights, liquidation rights, and other control rights respectively [9]. Pratt and Grabowski researched that venture capital returns come primarily from initial public offerings of the startups it invests in [10]. Carvalho has researched that the benefits of venture capital for enterprises also include non-economic factors, especially human resources [11].

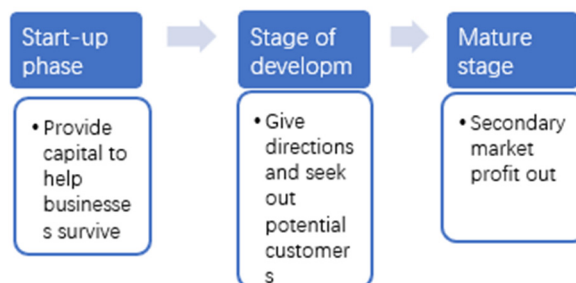
### 3. THE ROLE OF VENTURE CAPITAL IN PROMOTING TECHNOLOGY ENTERPRISES

#### 3.1 The contribution of venture capital in solving the fund problem of technology enterprises

Kochura's research shows that venture capital plays a positive role in financing knowledge-intensive enterprises. Venture capital also makes effort in promoting the stock market, retaining high-quality talents, and developing science and technology. Moreover, it helped the country and mankind become better [3]. In recent years, venture capital has become

more and more inclined to invest in high-tech enterprises, which has led to more and more technology enterprises going public. It also gets a glimpse of how venture capital solves the financing problems of technology companies through listed technology companies.

First, venture capital provides funds to support the development of enterprises at the start-up stage. This stage is fraught with risk, and only professionals have the gummy and ability to provide capital, primarily for the sake of huge future returns. At this point, the main role of venture capital funding for tech companies is to help them survive and support their further research. Over time, some tech businesses, for various reasons, are no longer viable, while others are stronger. At this time, the main role of venture capital is to help these surviving enterprises better manage, and for them to find opportunities for development, such as potential customers. Finally, with the help of venture capital, enterprises are better managed and more profitable. At this time, the conditions for enterprises to go public are ripe, and the role of venture capital is to help enterprises go public. After the listing of enterprises, enterprises have stable financing channels, and venture capital also gradually began to profit. To sum up, venture capital provides funding at the start-up stage when companies are very risky and exits when they mature and have stable access to financing.



**Figure 1** The role of venture capital in all phases

However, there is a certain amount of venture capital that will continue to invest after the company goes public, but this paper prefers to call it private equity. Just like what Caselli researched, the relationship between private equity and venture capital is more of a condescension. According to the research, venture capital is more inclined to enter early, while private equity is more like an investment behavior after the company matures. Private equity helps venture capital to obtain excess returns while also helping themselves to grab the profits of the company's sustainable development [5].

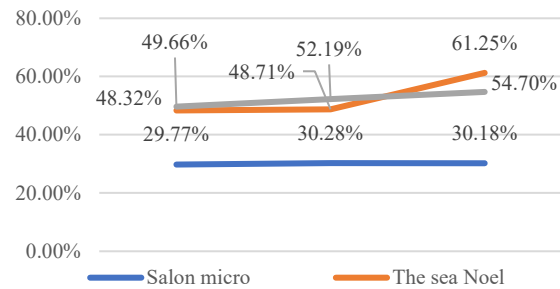
#### 3.2 The guiding effect of venture capital on the development direction of technology enterprises

From the research written by Gompers, it is found that with the difficulty of venture capital investment increases,

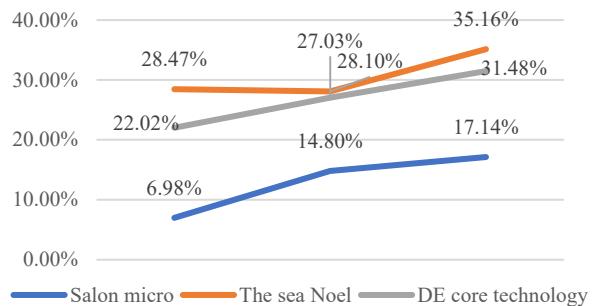
venture capital is more inclined to invest money in early high-tech companies, and venture capital use the information gap to analyze the situation of investable enterprises. Moreover, the venture capital is no longer a constant investment. After continuous tracking and detailed analysis of the company's situation, venture capital will selectively continue some projects and terminate other projects[8]. It can be seen that venture capital has enough information and data to judge whether a project will continue. Venture capital is also using this huge data to guide the direction of the enterprise. Venture capital helps enterprises find feasible development paths and connect with potential customers through information gaps. Carvalho has researched that the benefits of venture capital for enterprises also include non-economic factors, especially human resources.[11] In other words, venture capital not only guides enterprises in terms of development direction but also helps them in terms of human resources. Let's take JiMei Power as an example. JiMei Power was originally just an ordinary automobile battery manufacturer. After venture capital intervened in corporate governance, the company grasped the development tide of hydrogen energy and creatively applied hydrogen fuel cells to aircraft, achieving sufficient and stable profits. Venture capital helped JiMei Power survive and grow rapidly. At the same time, venture capital helped JiMei Power obtain several stable customers and provided funds to help further the research and development of JiMei Power, which helped JiMei Power develop in an all-around way. So in conclusion, venture capital is all-sided for enterprise guidance.

### 3.3 The effect of venture capital on the gross profit margin of technology enterprises

Kaplan and Stromberg researched that the significant characteristic of venture capital financing is that the venture capital capitalists are allowed to allocate cash flow rights, board rights, voting rights, liquidation rights, and other control rights respectively. [9] Through further research, it is found that venture capital now not only provides capital to startups but also participates in the strategic planning and financial coordination of startups. Furthermore, venture capital not only guides technology companies in terms of direction but also plays an indispensable role in improving their gross margins, especially in the year before their initial public offerings. Here are the gross and net profit margins of randomly selected tech companies that are about to go public in China. They all have venture capital on their shareholder lists.



**Figure 2** Gross profit margin (%) three years before listing



**Figure 3** Net profit margin (%) three years before listing

From these figures, it can be seen that its gross profit margin and net profit margin increased year by year after venture capital joined the enterprise, especially in the year before its listing. It can also be seen that venture capital plays a great role in the improvement of gross and even net interest rates of technology enterprises. The reason is that venture capital plays a significant role in enterprise cost management and sales promotion. At the same time, venture capital has helped companies navigate perilous start-up stages, gain scale and build a reputation. Under the dual effect of brand effect and scale effect, the gross profit margin of the enterprise is naturally improved. As mentioned above, when venture capital guides enterprises in all aspects, it will naturally help enterprises increase earnings.

## 4. THE CHANGE OF VENTURE CAPITAL INVESTMENT DIRECTION IN RECENT YEARS

After explaining the role of venture capital in promoting technology companies, let's focus on the changes in the direction of venture capital investment in recent years so that investors can make investment judgments based on the trends.

### 4.1 Changes in the field of venture capital and investment advice

In recent years, the field of Venture capital in China has changed a lot. As the Chinese government's focus shifts from real estate and finance to big technology,

venture capital in China in recent years has also moved closer to high-tech enterprises, mainly advanced manufacturing. A total of 387 Chinese companies have registered to go public, including 216 in the manufacturing sector. In the advanced manufacturing industry, the most investment potential is lithography machines and industrial machines. These are two of the most limited areas in China's technological development, and they are the path the country must take as it tries to acquire high-value-added industries. At the same time, because foreign Chinese enterprises have great technological advantages in these two fields, it is very risky to invest in these two fields. Whether venture capital can help Chinese enterprises breakthrough technological barriers is the key to obtaining excess returns. By analyzing the data, it is noticed that venture capital is looking at another area -- healthcare. As China's population ages, medical resources are also the next potential source of high profits. However, as basic medical care has been saturated, venture capital should focus on high-end medical care. Next, let's interpret the trend of venture capital investment through the trend of listed companies.

## 4.2 Information about Listed Companies

### 4.2.1 Listed company data statistics

More and more companies have sprung up in recent years, and some of the best have gone public for the first time. Pratt and Grabowski researched that venture capital returns come primarily from initial public offerings of the startups it invests in.[10] As venture capital returns come primarily from initial public offerings of the startups it invests in. Therefore, the investment trend of venture capital will gradually converge with the type trend of listed companies. So, what kind of companies a country needs to go public is the trend that venture capital needs to follow and the reason why venture capital benefits the country. Therefore, this paper has compiled the data of listed companies after 2020 to summarize the trend of listed company categories. These data are from Wind, Enterprise check, and enterprise annual report.

In the past two years, the type of listed companies was mainly in the manufacturing industry, the number has reached 97. Information technology services followed with 23. And there are only two financial companies.

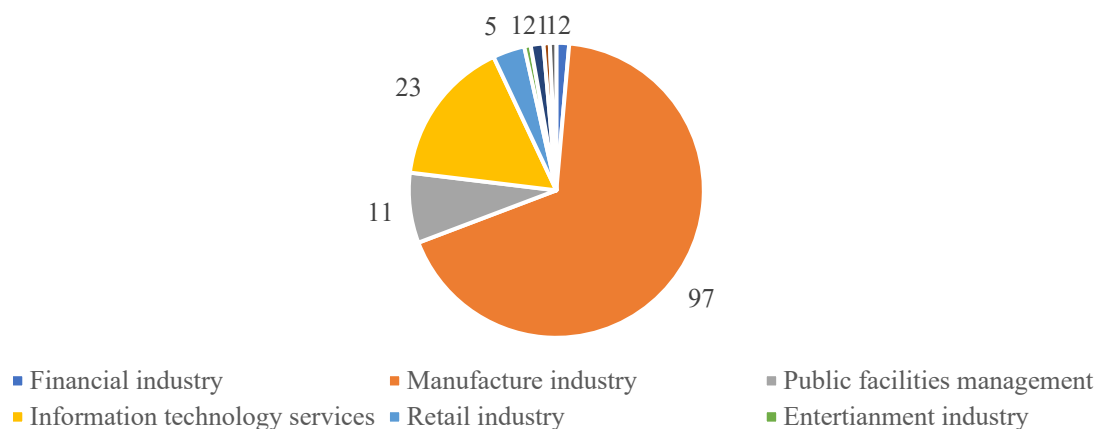


Figure 4 The type of listed company

This proves that in recent years, venture capital is shifting from finance and real estate to information technology services and manufacturing.

### 4.2.2 High-tech company information statistics

Through the statistics of the company's gross profit margin in the past year. This paper considers a company with a gross margin of 20% or more to be a technology company. And this paper takes the Chinese government's new list of specialties as proof of their technological content. This paper determined these figures through an analysis of corporate annual reports

From the figure above it can be found that there were 114 first listed high-tech enterprises in the past two years, and the average gross profit rate of these listed enterprises reached 31.65%.

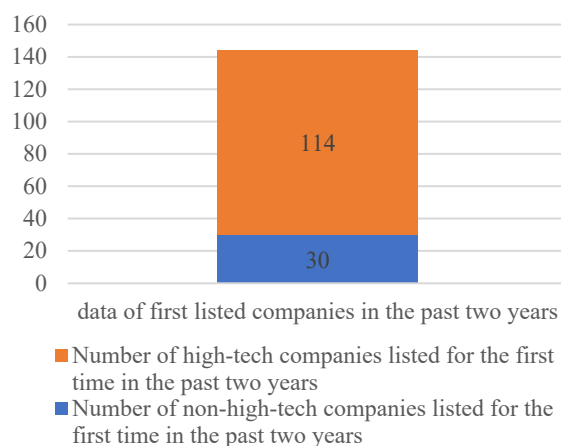
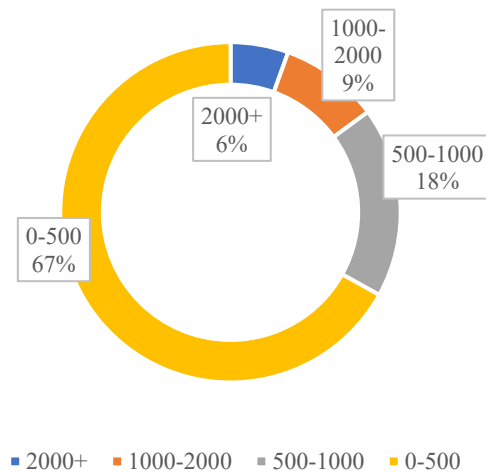


Figure 5 Science and technology content of listed companies in the past two years

As it can be seen from the chart above, the tech content of first-time public companies in the past two years is very high.

#### 4.2.3 Statistics on jobs created by enterprises

Through the statistics of the number of social security published by enterprises, the number of jobs created by businesses can be roughly calculated. But the number of jobs created is higher because of outsourcing and unstaffing. By counting companies' contributions to social security, this paper gets the number of jobs created by first-time public companies over the past two years. For a few of them, there was no way to get the number of people who paid Social Security contributions publicly, and this paper substituted that for the average number of jobs created by other companies.



**Figure 6** Jobs created by first-time public companies

These companies created an average of 666.74 jobs and a total of 96,010.56 jobs. Because of the outsourcing and non-contract workers, the actual number of jobs created is much higher. This will give a big boost to social employment. Overall, the listing of these companies has brought great benefits to society, they also helped venture capital flourish.

## 5. THE CHARACTERISTICS AND CHANGES OF VENTURE CAPITAL

### 5.1 The nature of venture capital

Venture capital is a high-risk, high-return investment, Cochrane researched that venture capital bears high risks as well as high returns, but its risks are acceptable and cover the demand for returns [6]. In other words, venture capital seeks a few success stories from a large number of investments. In pursuit of such rare success stories, venture capital is tightly managed inside, Through Sahlman's research. It is found that the original capital of venture capital mostly comes from individuals and

organizations, and its investment preference is mostly high-risk and high potential early enterprises. The internal organizational structure of venture capital is rigorous and complex to achieve the purpose of high efficiency and high returns. [7]. Therefore, for venture capital, choosing the right industry with adequate capital and management is the way to success.

### 5.2 Changes in the location of venture capital investments

Venture capital investment location is changing from developed countries to developing countries, from localization to globalization. Tohmatsu finds that nowadays people live in a globalized world, and venture capital is gradually expanding from local investment to global investment, to adapt to the tide of globalization and get more lucrative profits [4]. Looking at all the developing countries in the world, China is undoubtedly one of the countries with the greatest potential. As a result, China has been a destination for venture capital investment in recent years. For venture capital, choosing the right industry is important, as is choosing the right location. Wong and Anson's research has shown that venture capital has boomed in China over the past three decades. In the beginning, it was led by foreign institutions and gradually became the joint efforts of foreign and domestic institutions. At the same time, investment is shifting from information technology to financial services. Also, the type of VC investment mostly ventures capital (59%) [2]. The flourishing of venture capital in China proves the superiority of venture capital globalization and investment in developing countries. In the future, as China gradually matures, venture capital's investment in China will gradually shift from comprehensive to partial industries, and countries such as Southeast Asia and India will become the next region that venture capital can focus on.

### 5.3 Problems with venture capital

Sahu et al. researched private equity and venture capital trends in recent years. Private equity has expanded into more areas in recent years, helping companies create value while making big profits through efficient exits. Also, venture capital tends to invest in developing countries and emerging areas, but it is increasingly constrained in developing countries [1]. This research shows that as countries prosper, venture capital opportunities tend to become structural, meaning that only some industries have good returns. Venture capital will also face increased regulation. Therefore, venture capital needs to constantly update its knowledge, constantly follow the national development strategy, and constantly strengthen its supervision, to stay sustainable. To sum up the problem of venture capital in one sentence: there is never a shortage of money, only a shortage of people who are good at using it.

## 6. CONCLUSION

By analyzing the trend of Chinese listed companies in recent years, this paper finds the change in venture capital investment trend. In recent years, venture capital is more inclined to invest in high-tech enterprises, especially high-end manufacturing and the high-end medical industry, which is very consistent with the development strategy of the country. At the same time, venture capital plays a very important role in the financing and development of enterprises. Venture capital guides enterprises in all aspects, from the capital to human resources, from enterprise management to direction selection. This help allows companies to grow and go public successfully, benefiting society and helping venture capital make profits. So, the growth of venture capital and country are mutually reinforcing. But as the country has prospered, so have restrictions on venture capital. In the future, venture capital needs to do the following. First of all, venture capital needs to broaden its investment horizon, change from localization to globalization, and extend its application from developed countries to developing countries. Second, venture capital needs to clarify its governance regime to cope with increased regulation. Finally, venture capital needs to understand its social responsibility, follow the pace of national development, and conform to the trend of the time, to be sustainable. In terms of investment, taking China as an example, I think venture capital needs to focus on lithography machines, industrial machines, and high-end medical care. And globally, the development of new energy should be more attractive, such as HJT batteries.

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