Influence of Fiscal Policy on Venture Capital Investment from Its Development in China

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Abstract: China’s fiscal policy that supports the development of venture capital investment can mainly be divided into direct fiscal policy and indirect fiscal policy. The different fiscal policy must impose different influences on venture capital investment. Based on the overview of venture capital investment, the influence of direct and indirect fiscal policy on development of venture capital investment is elaborated in this paper.

Key words: Venture capital investment; fiscal policy; influence

China’s venture capital investment, started in the mid 1980s, has had a considerable development from nothing and from messy to standard. However, the small scale, weak strength and insufficient capital investment of venture capital investment enterprises lead to low percent conversion of scientific research achievements, single capital source and significant administrative orientation of government. China’s risk investment enterprises are hard to take a road of rapid development if the above problems are not solved. The author thinks to develop the venture capital investment enterprises in China and promote the further development of high-tech industry, the government should refer to the western advanced experience, combine China’s national conditions and current situation of development of venture capital investment and give full play to the influence of fiscal policy.

I. Overview of venture capital investment

From the investment behavior, venture capital investment mainly refers to the investment process that the capital is input in the high-tech technology and product R&D field with high failure risk and then the high-capital benefits are obtained by promoting the commercialization and industrialization of high-tech achievements. From the operation mode, venture capital investment mainly refers to the process that the investment intermediary managed by the professional talents inputs the relevant venture capital to the high-tech enterprises with great potential. This is to control the relationship between venture capitalist, technician and investor and also the important investment mode of benefits and risk sharing.

II. Influence of fiscal policy on venture capital investment

In addition to create better development environment for venture capital investment with relevant legal systems, the governmental department should use the corresponding economic means, that is, relevant fiscal policy, to participate in the decision preference and decision behavior of the subject of venture capital investment market so as to promote the better development of venture capital investment. The fiscal policy adopted by the government for
venture capital investment is mainly divided into direct fiscal policy and indirect fiscal policy, which impose different influences on venture capital investment.

(I) Influence of direct fiscal policy on development of venture capital investment

First, positive influence of government’s direct fiscal policy. The government’s direct fiscal policy mainly refers to the government’s direct investment or government’s fiscal subsidy that drives the development of venture capital investment. Government’s fiscal fund is to provide seed fund for risk enterprises to bear the corresponding investment risk caused by venture capitalist and make the current venture capital investment project have long-term sustainable development. Thus, the risk enterprises in the embryonic stage or in the initial growth stage can get powerful financial support so as to directly promote China’s venture capital investment industry to have new development. The government fund can use the interest display mechanism to improve the high benefits of venture capital investment, which will play a demonstrative role in the private capital to guide more private capital to conduct venture capital investment. The government’s financial fund can tap a large number of high-quality risk projects to reduce the risk of venture capital investment and improve the benefits of venture capital investment. In addition, the model demonstration can be used to attract more fund into venture capital investment. At the same time, once the venture capital investment conducted by the government is successful, the private capital will really realize the high benefits of venture capital investment so as to practically reduce the expected risk of venture capital investment and increase the preference of venture capital investment. In addition, the capital obtained by the government in venture capital investment can make the venture capital investment industry have rapid development and can cultivate a large number of high-quality venture capital investment talents and accumulate rich experiences in venture capital investment operation so as to improve the success rate of venture capital investment. Therefore, the direct input of government in venture capital investment can play a great demonstrative role and multiplier effect to attract and drive more private capital into venture capital investment.

Second, negative influence of government’s direct fiscal policy. The government’s direct fiscal policy has positive influences on venture capital investment and also has deficiencies, which may cause negative influences on venture capital investment to a certain degree in case of improper use. Under the circumstance that the total resources are fixed, the government’s direct investment can increase the fierce market competition in talents, project, product and other aspects, improve the cost of venture capital investment and practically control the expected profit of venture capital investment so as to form crowding-out effects when the private capital participates in venture capital investment. First, the direct investment of governmental department in venture capital investment can attract more venture capital investment talents and entrepreneurial talent, which will increase the buyer-level competition in the human capital market of venture capital investment to increase the price of human resource so as to increase the human cost of private capital’s participation in venture capital investment; second, in the direct investment of governmental department in venture capital investment, the subject will preferentially choose the high-benefit, low-risk and high-quality risk control project due to the intrinsic benefit-tending and harm-avoiding tendency to aggravate the buyer-level competition in the risk project market so as to improve its service price under the condition that the short-term supply of service intermediary is unchanged and the intermediary cost that the private capital participates in the venture capital investment will increase correspondingly.
(II) Influence of indirect fiscal policy on development of venture capital investment

The governmental department’s indirect fiscal policy for venture capital investment means that the government guides the decision preference and decision behavior of the subject of venture capital investment market by using indirect economic regulation and control means to promote the development of venture capital investment. The direct fiscal policy mainly includes tax policy, government guarantee and government procurement.

First, influence of tax policy on development of venture capital investment. Tax is an important lever in the national macro control system and also the primary means for the government to implement macroeconomic control, with legal attribute. Under the market economy conditions with Chinese characteristics, the tax coordinated with various form and price mechanism will affect or determine the direction and scale of social investment to a great extent. When the market subjects compete under other conditions with the same market conditions and environment, tax burden and tax preference will directly affect the choice of investment. Therefore, tax policy does not have positive effects, but also have negative effects. In case of insufficient investment, the governmental department can implement tax preference policies to practically reduce the tax burden and investment cost of investors to encourage the investors’ investment initiative so as to stimulate the investment behavior and increase the investment. In case of over-investment, the state can implement restrictive measures in tax, such as increase of tax burden and reduction of tax to make the investors reduce investment. Tax policy have an incomparable function in the development of venture capital investment compared with other economic means due to the intrinsic attribute of tax and its investment adjustment function. Generally, whether the venture capitalist invests in the high-tech industry mainly depends on the expected benefits of venture capital investment and measurement of investment risk and the venture capital investment is conducted only when the expected benefits are higher than the risk. The expected benefits of venture capital investment and its risk greatly depend on the policy in tax. Once the tax, especially the capital gain tax and enterprise income tax, reduces the investment benefits and investment returns of investors, the investors will turn to the investment field with small risk and stable benefits, thus, the initiative of venture capitalists can be controlled, which can affect the development process of venture capital investment enterprise. Once the state gives more tax preferences to venture capital investment enterprises by tax policy to make the enterprises have light tax burden, reduce their investment cost and risks and improve their after-tax profits and investment benefits, the venture capitalists’ initiative can be protected and mobilized, thus continuously increasing the input of venture capital investment, so the venture capital investment industry will have rapid development. Driven by the expected huge economic benefits, many market economy subjects will show strong willingness to venture capital investment industry to make social capital transfer to venture capital investment industry.

First, influence of government guarantee on development of venture capital investment. Due to the unique position of bank in accumulating the social idle fund and the insufficient risk tolerance, countries all over the world generally adopt the government guarantee. For example, the United States set up SME Administration early to be responsible for the bank load guarantee required by medium and small high-tech enterprises. Then, the United States specified that the bank loan of risk enterprise could be up to 90% of the total project investment by act, so the government would compensate for 90% of the losses in case of bankruptcy of enterprise. As the interest of guarantee and financial institutions in small enterprise investment increased.
continuously, the loan amount of small enterprise increased rapidly. Ministry of International Trade and Industry set up R&D Enterprise Cultivating Center in the mid 1970s to be responsible for providing corresponding debt guarantee of bank loan of risk enterprises, with a guarantee proportion of up to 80%. At the same time, Japanese government directly established the credit guarantee association for credit guarantee and SBCIC fore re-guarantee of guarantee association. The credit guarantee is the combined product of credit proof and asset liability assurance. The government guarantee of venture capital investment risk can improve the credit line of startup company, form good bidirectional relationship between startup company and bank and establish effective risk sharing system so as to greatly reduce the risk between creditor and debtor. With the government guarantee, the state can drive a large number of bank capital and private capital to input into the risk enterprise with a little capital by using the lever principle. Therefore, the government credit guarantee is often called the important “amplifier” of risk capital and the practical experience of many countries proves that the amplification can be up to 10-15 times.

First, influence of government procurement on development of venture capital investment. As an important mean that the fiscal policy affects the specific production operation behavior of enterprise, the government procurement means that the governmental department inputs the financial fund into the enterprise consciously to be conducive to the weak links in the economic operation so as to create better development opportunities for enterprises. The government can provide a large number of preferential policies to enterprise by changes of purchasing object and purchasing price to make enterprise get high profits by bulk purchasing and produce a role of policy guidance of government procurement. Venture capital investment is to get high returns by increasing the investment in high-tech enterprises to realize the marketization, commercialization and industrialization of scientific and technological achievements. The features of venture capital investment determine that high-tech enterprises generally face high risks in market, technology, operation and decision in the development process and the market risk is concerned by venture capitalists due to the high investment, high risk and other features of the marketization, commercialization and industrialization of high-tech achievements, which should be supported by high benefits, but the benefits are finally realized by market. Once the high-benefit market is not smooth, not only the marketization, commercialization and industrialization of scientific and technological achievements cannot be guaranteed, but also the high returns of venture capital investment cannot be gained. Considering this, the government procurement system should provide corresponding market support and protection for high-tech enterprise so as to promote the sound development of China’s venture capital investment industry.

III. Conclusion

In conclusion, due to the features of venture capital investment and its importance in the economic development, it is an internationally accepted practice that the government supports the development of venture capital investment by using direct fiscal policy and indirect fiscal policy. The government’s direct fiscal policy plays a guiding and demonstrative role in venture capital investment, but considering the bad effects caused by the direct participation of government capital in the venture capital investment, the government should comprehensively consider the function of government in the resource allocation in the application of direct fiscal policy and then use its direct venture capital investment can be used to improve the reasonableness of resources allocation on the basis of improving the market allocation efficiency. Therefore, the government’s direct financial investment does not compete with the commercial venture capital investment, but
supplements and cooperates with it. The bad influence of direct fiscal policy proves from other perspective that the direct promotion of the development of venture capital investment by relying on fiscal expenditure in a traditional sense will be restricted, but the indirect financial means that the government supports the venture capital investment has few limitations and can play important role in supporting the development of venture capital investment.

References: