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Angels Investing the Big Picture

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LearnLaunch

Launchpad, Golden Seeds & Hub Angels

Introduction

- An entrepreneur needs capital
- Angel investors would like to invest in situations that have the potential of high returns
- Angel investors would like to support local/regional entrepreneurs
- This session will:
 - A. Position angel investing in comparison to other asset classes and review investing strategies
 - What funding works for various types of companies
 - B. Review the process by which angels and entrepreneurs get together, work together, and then part company
 - C. Discuss learning to be an angel
 - Look into New England ecosystem for angel investing

Overview

Overview of Funding Sources

Angel Investing Process

Angel Investing .. Important part of the process

What investors need to know about a company to decide

Entrepreneurship comes in many forms

SOCIAL VENTURE COMPANY

- Goal is to fulfill a social need
- Has mission orientation
- Team needs to support mission
- Can have normal or high growth profile
- Exit ...maybe harder to find fit

NORMAL GROWTH COMPANY

- Includes all service businesses
- Exploiting a local market need
- Team has 'great jobs'
- Grows revenue in direct proportion to # employees, or has low profits
- Exit will be based on value of cash flow (mature biz.)

HIGH GROWTH COMPANY

- Company can grow fast (on-line) or has a scalable system
- Team often motivated by exit
- \$7-10M revenue in 5 y & market size allows significant additional growth
- Capital efficient total investment \$2-4M
- Exit by M&A

EXTREME HIGH GROWTH COMPANY

- Growth profile ultra-scalable
- Team focus is exit
- Revenue \$40M+ with lots of room for growth (5 yr.)
- Based on \$20M+ investment
- Exit targeted to IPO or by 'large' M&A event

Entrepreneurship comes in many forms

SOCIAL VENTURE COMPANY

- Friends family, founders
- Charity\$\$
- Crowd funding (Kickstarter)
- Impact Angels
- Impact VCs & family offices
- Crowd funding (portal style)
- Royalty based debt

NORMAL GROWTH COMPANY

- Friends, family, founders
- Debt, Bank, and other
- Growth debt
- (Future) Crowd funding (portal style)

HIGH GROWTH COMPANY

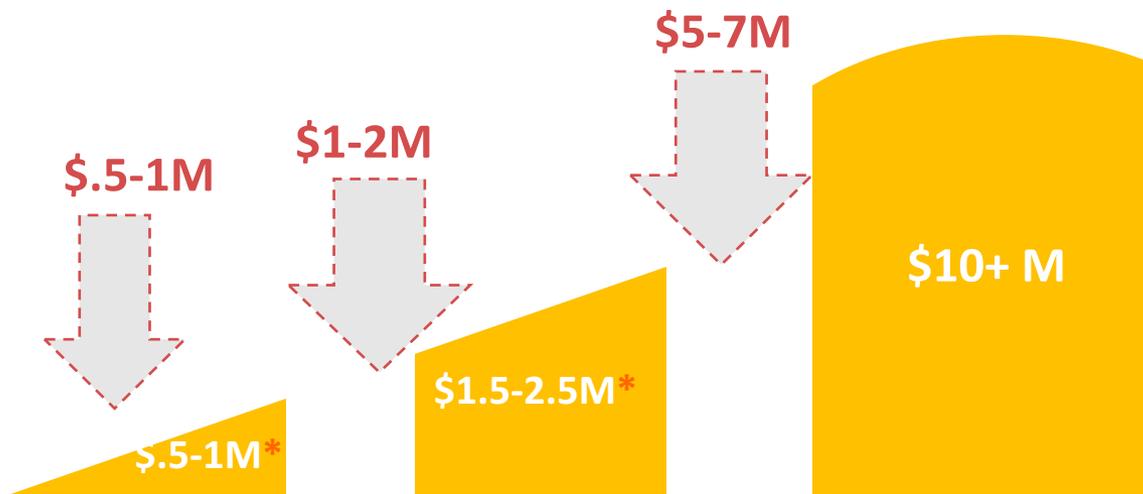
- Angels
- Angel Groups
- Angel Group Syndication
- Angel List
- Micro-cap Funds
- Crowd funding (portal style)
- Venture Debt
- Strategic Corporate VCs

EXTREME HIGH GROWTH COMPANY

- Early on
- Accelerators
 - Individual Angels
 - Micro Cap VCs
 - Seed from VC
 - Venture Debt
- Later stages
- Venture Funds
 - Strategic VCs
 - Angel Syndication

Crossing chasms

High growth companies are **not profitable enough** to invest in deep customer support, increasing expensive sales & marketing efforts, and new products, **all at the same time**, so they need to scale the company with **other peoples money**



Moving forward:

Sales process → single, multiple to regional

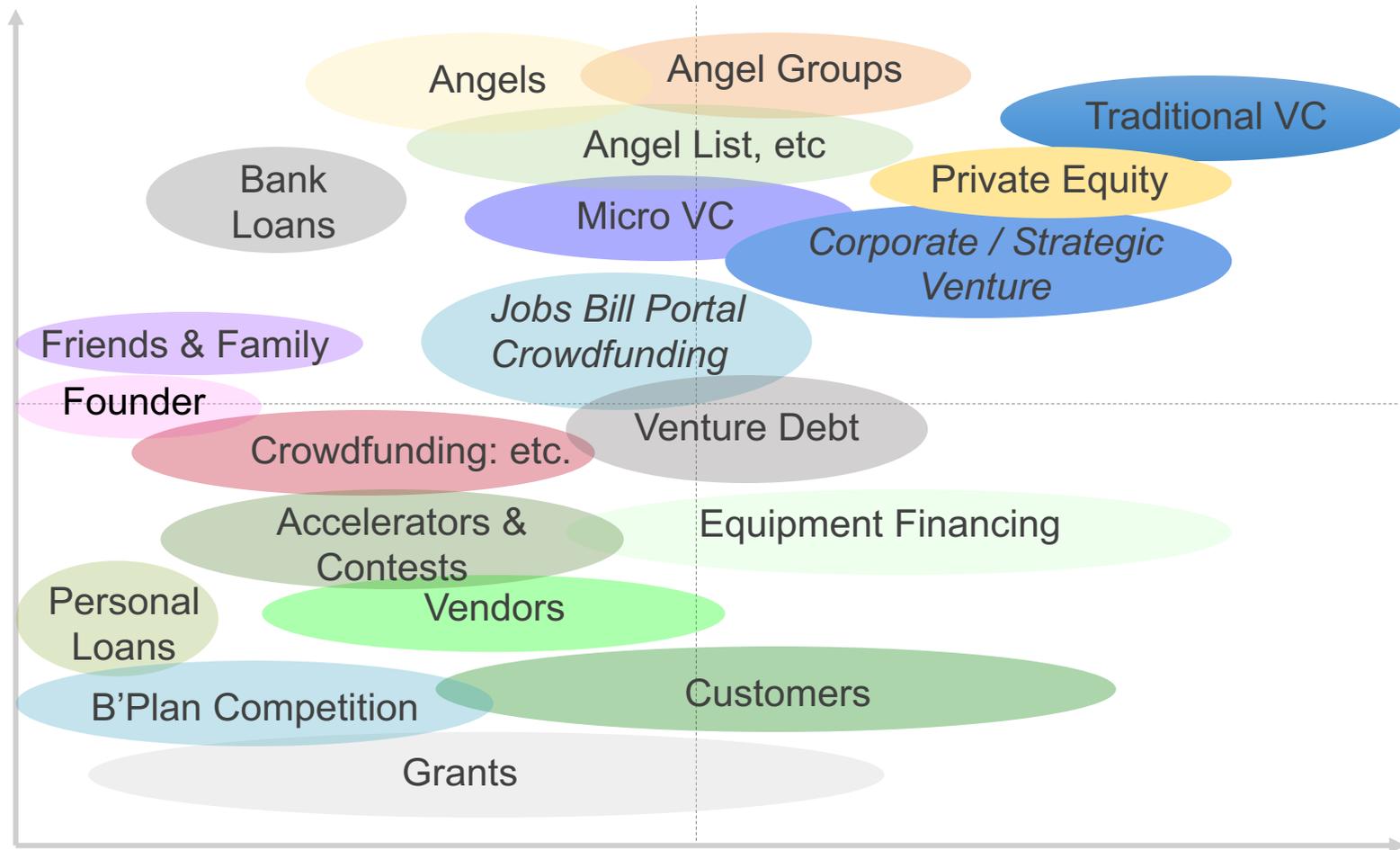
Personnel → everyone does everything, specialist to development of human capital

Processes → logical guess/react, opportunistic to drive/lead market

→ Every company's financing path is **unique**

* **Annual revenue or annual bookings with increasing repeatable revenue model**

Capital Sources



Entrepreneurs usually build a personal path through many sources

Angel Investment Process

Investment Cycle



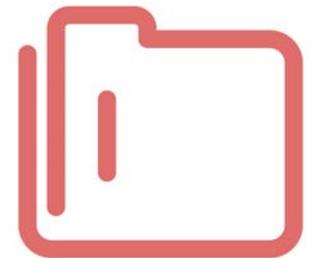
**Develop
Strategy**



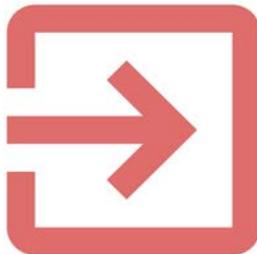
**Source
DD &
Invest**



**Manage
Follow-On
Rounds**



Exit



What is a Business Angel?

- A Business Angel is an accredited investor who invests his/her own capital in private companies – usually early stage companies
- Angels invest on their own, in crowd funding or in organized groups
- Angel investments can be small (\$5k) or very large (\$1m)
- Collectively, angels are a tremendous source of capital for private companies
- Alternative early stage investors include:
 - Crowd funding (Kickstarter) Incentive style
 - Crowd funding (Job Bill Portals)
 - Accelerators
 - Micro-cap VCs
 - Institutional VCs



*These individuals are nearly always “accredited investors” as defined under the Securities Act of 1933

What do you know bout angel investing?



**"I used to provide capital for business startups.
Here's my card. I'm an angel investor."**

What Motivates Angels: Financial Return

- However, there is a lack of “Clean Data” from angel returns
 - The Angel Capital Association Halo Report, UNH Venture Center
 - Most estimates suggest VC-like returns...these approach 3X for successful funds, with IRRs above 20%
- Portfolio effect is significant
 - Recent analysis of ACA data suggests that at least 6-7 investments are required to cross into “expected positive exits”, with 12 or more over 5-7 years showing an even greater likelihood of significant returns
 - Participation in later rounds can have a large, positive effect

Fund Type	1 Yr	3 Yr	5 Yr	10 Yr	20 Yr
Early/Seed	(20.6)	1.7	3.7	36	21.8
Mezzanine	(26.9)	4.6	8.4	13.5	14.5
Later	(6.8)	9.5	8.7	7.5	14.5
All Venture	(20.9)	4.2	6.4	15.5	17.0
NASDAQ	(38.1)	(10.3)	(4.6)	(3.2)	7.3
S&P 500	(36.1)	(10.0)	(4.0)	(3.0)	6.1

What Else Motivates Angels

- Many angels are involved with mentoring, coaching, training and advising entrepreneurs – or even finding their next job
 - Some with a focus on their own portfolio
 - Some to help all entrepreneurs
 - Lots to help area organizations in the eco-system
 - Or to find a full or part time position
- Many companies provide a small number of options for advisors & board members
 - When averaged with your investment ... these have a big effect on returns at exit
- Learning, and staying up to date on new technologies and business models
- Creating companies creates jobs, wealth, etc.
- Good for economy

- Networking and socializing

This Angel Group Seems Right

- Investment philosophy
 - Similar risk tolerance and return goals
 - Stage, capital requirements, size of market, etc.
 - Similar behavior norms
 - Lots of complete diligence written up vs. little diligence
 - Lots of ‘expert-lead investing’
- Structured or unstructured
 - Club/Network, Fund, Sidecar Fund
- Pace of investments
 - Number of meetings (day/time/location), companies per session, investments per year
- Quality of the people and network
 - Find people who are fun to be around and work with

An Angel Group: It's a Group

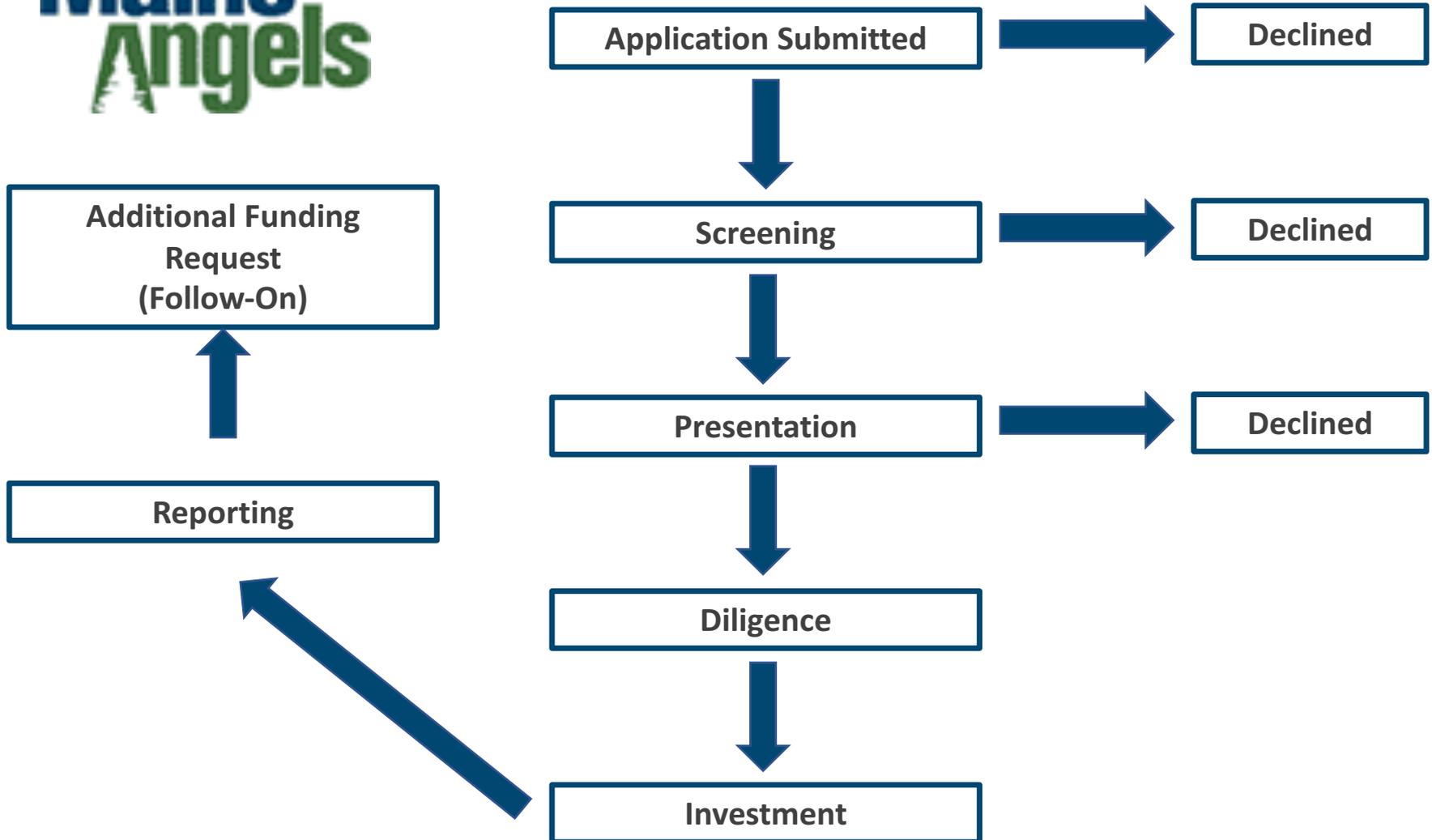
- Takes work to keep the group going and growing
- Group decision making can fill in the knowledge gaps
 - But first complainer has a lot of power
- Finding fun sub-groups can speed the work
 - Who does what
 - Who is fast and accurate
- Can be a lot of fun
 - Meet people to focus on real business problems

Steps in the Angel Group Investment Process

- Find an Interesting Company
- Screen the Company
- Company Presentation to Members at Group Meeting
- Due Diligence
- Potential “syndication”
- Negotiate Deal with Company and Make Investment
- Support & Monitor the Investment (e.g. Corporate & Advisory Boards)
- Exit (e.g. IPO, M&A, Dividends/Royalties or Shutdown)
 - Slides 18- 29 are here ‘as notes’
 - There are lots of little steps

Application Process

*Maine Angels = Online Application



Where do Angel Groups find Interesting Deals?

- Members of your Angel Group
- Other Angel Groups or Independent Angels
- Venture Capital Firms
- Service Providers (e.g. lawyers, accountants, etc.)
- Incubators and Accelerators (TechStars, LearnLaunch)
- Networking at Local Technology Centric Events
- Over the Transom (e.g. direct from the entrepreneur)
- **Over time everyone in a group needs to be able to say what fits and what doesn't**

Screening

- Are we interested at all? – Are geography, industry, stage, valuation all OK?
- Does it make sense?
 - Does the total need for capital match the opportunity?
 - Can the team carry it off, with appropriate help?
 - Does our group have any applicable industry experience?
- Are there unanswered questions for follow-up before a decision?
- Is there likely to be general interest in this, or is it very specialized?
- Often, first 30 seconds with company's documents will tell all you need to know
- Many angel groups increasingly focus on screening to improve results

Presentation

- If it passes screening, company is invited to present to whole group
- Presentations are usually 10-15 minutes followed by 10-15 minute Q&A
- Presentation should cover the following items:
 - Problem to be solved, company solution, market opportunity, go-to-market plans
 - Management team, competition, current status, financials, funding needs & likely deal
- If there is interest from “enough” members, we proceed to due diligence

Due Diligence*

- The point of due diligence is to give the deal an appropriate (due) level of scrutiny so that the group as a whole can make intelligent investment decisions. As a part of the process, it develops an interested cadre of potential investors.
- Form the team with at least one industry knowledgeable member
- Assess the company so less involved members and syndication members can decide
 - **The 'work'**
 - **We will look at this later**

Finish Diligence and Outline Deal

- Assuming the key questions are answered satisfactorily finish diligence including:
 - Check references on team
 - Check market on product – users or prospective users
- Start Deal:
 - Start negotiation of valuation and general deal terms
 - Develop term sheet
 - Think out next rounds and locate “best” board member
- Report back to group and check on its interest; make an educated guess at total \$ interest

Company Assessment

Diligence Factors

Leadership Assessment

Technology, IP & Product Roadmap

Regulatory Strategy

Customer Need & GTM Plan

Uniqueness & Competition

Market Size & Market Opportunity

Financial Projections & Funding Strategy

Exit Strategy

- 1. Risk / Return assessment**
- 2. Match to the human capital and capital available to this deal**

Syndicate the Deal

- Often a single group cannot or will not fund a complete round so syndication is required to get the necessary funding
- New England groups work through the “Angel Treaty”, which greases the syndication skids
- Interests and diligence requirements differ from group to group, so more diligence may still be asked for in syndication
- There is little “shopping” of deals in the NE angel ecosystem
- No interest in group A neither implies that group B will not be interested, nor that members of group A won’t invest if group B endorses a deal

Term Sheets*- Summarizing the Deal

- Based on standard terms found in many early stage venture deals
- Provides a high level overview of key deal terms
 - Type of Security: Preferred Stock, Convertible Note, SAFE etc.
 - Financial Terms: Valuation, Dividends, Liquidation Preferences
 - Corporate Oversight: Board of Directors, Voting & Information Rights
- Written by either the entrepreneur's or the investor's attorney
- Often signed by the entrepreneur and a representative of investor group
- Not usually binding on either side, although the entrepreneur can't use it to look for a better deal elsewhere

Legal Documentation

- Once a term sheet is signed and due diligence is complete, work begins on preparing complete legal documentation
- Documentation varies based on type of security
 - Convertible Notes (short and simple), Preferred Stock (lots of paper)
 - Includes: Investor Rights, Voting, Co-Sale & Stock Purchase Agreements
- Documents are prepared and reviewed by attorneys on both sides
- Typically, each investor signs appropriate documents
- Fees for investors' counsel are paid by the company out of the proceeds of the investment

Closing the Deal

- Final legal documentation is sent out to all interested investors
 - Usually with very explicit instructions on what to sign and where to send signed documents and invested funds
- Signature Pages are signed and mailed along with a check
 - Documents are sent either to company or to lead investor
 - Funds are sent either by check or wire transfer
 - In some cases, funds and documents are held in escrow until full investment is received
 - In some cases, a rolling close is used to distribute funds to a company while new investors are brought in to the deal

Monitoring the Investment - Individual

- As an individual investor
 - Read the quarterly or annual reports
 - If you don't understand something, ask – there are no dumb questions
 - If you have a suggestion, email or call the CEO or your investor representative

Monitoring the Investment – Group Rep

- As the group's “representative*”
 - You'll probably sit on the Board of Directors
 - Take this seriously. You have fiduciary obligations to many people -- to all stockholders, employees, vendors, customers, etc. -- not just “your” investors
 - This can sometimes lead to long and difficult unpaid hours, particularly if the deal has troubles. You must be prepared to put in the effort under all circumstances
 - Read the Board materials and attend all meetings
 - Be a resource for the CEO. Being in charge can be lonely and the Board members can help
 - Consult with other investors as needed
 - Take an appropriate fee (sometime a stock option) for your service
 - *each investor has direct relationship with company

Exits: Good & Bad

- Good exits
 - Likely the largest deal the CEO has ever done
 - Offer help if appropriate
 - If it's not appropriate, stay out of the way; it's a stressful time
 - If the amounts involved are large, it might be worthwhile to hire an outsider to check the numbers or be an exit advisor
 - Deals are complex, mistakes happen (several investors might band together to pay for this). This is particularly applicable if many layers of investment came after yours
- Bad exits
 - Grin and bear it
 - If you invested in equity (not convertible debt) make sure your tax advisor looks at Section 1244
- **IPO, M&A, Dividends/Royalties or Shutdown**

Due Diligence: Critical to New England's Angel Ecosystem

- Innovation in our region is unique & dynamic
- Angel investing is growing in quantity and quality
- Angel groups are becoming more sophisticated
- Syndication among groups is growing, and is a critical component of the angel industry's development
- Syndication reduces the amount of time and effort involved in raising capital for an investment opportunity -- angel treaty
- **Successful investing, within groups and syndications, has due diligence sharing at its core**

Angel Investing

Important Part of Company Creation

Trends: More Private Funding

TRENDS

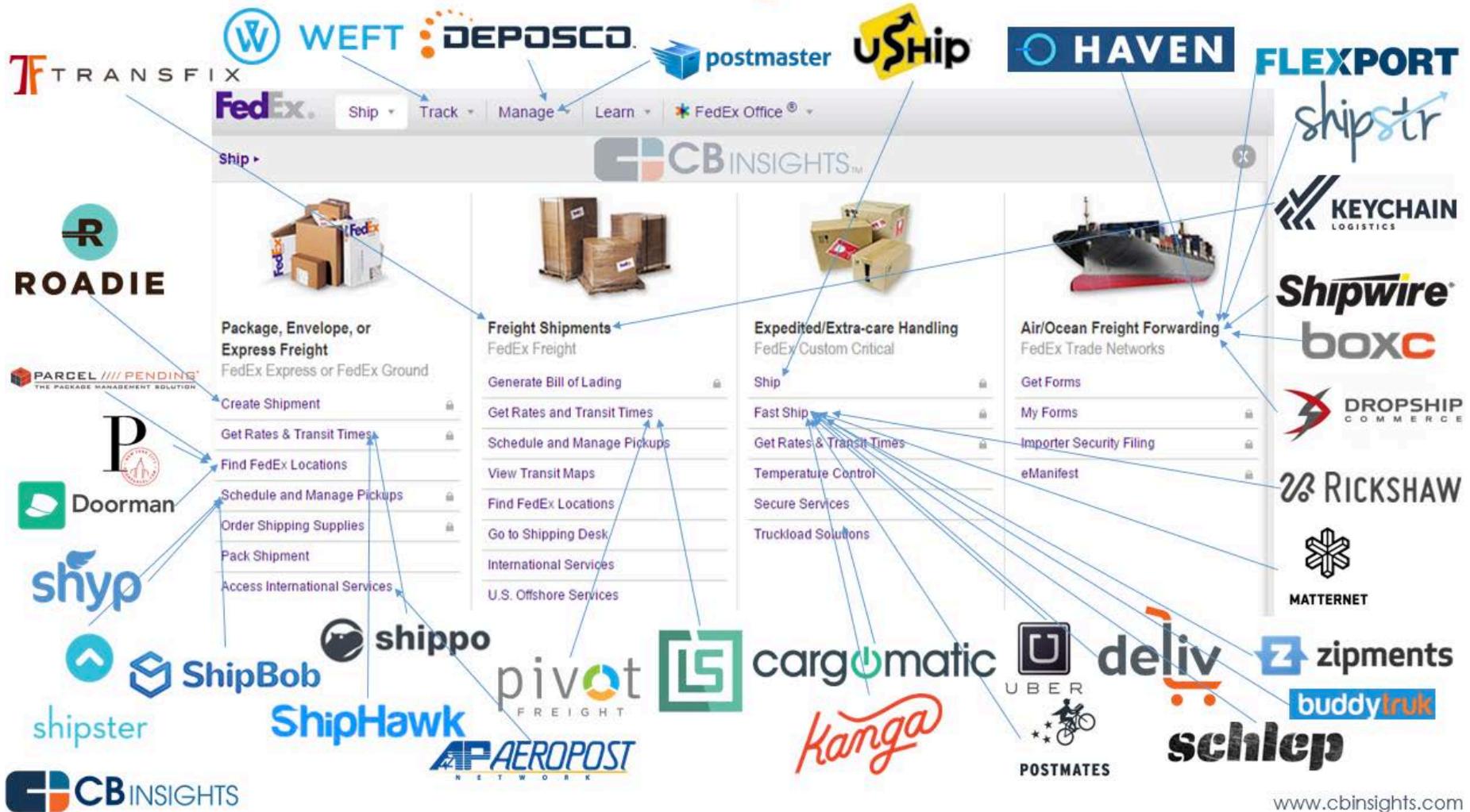
- Companies get started: look for market traction
- **Any industry can be disrupted! Not all disruptive companies can grow and exit**
- Cost to start companies at all times low (co-working, cloud, development suites, etc.)
- **Angel funding is top of funnel in various styles**
- But the search for Series A level funding continues to be hard
- Capital flight to late stage VC
- PE both growth and buy-out are at all time high
- IPOs at historic lows

MARKET RESPONSE

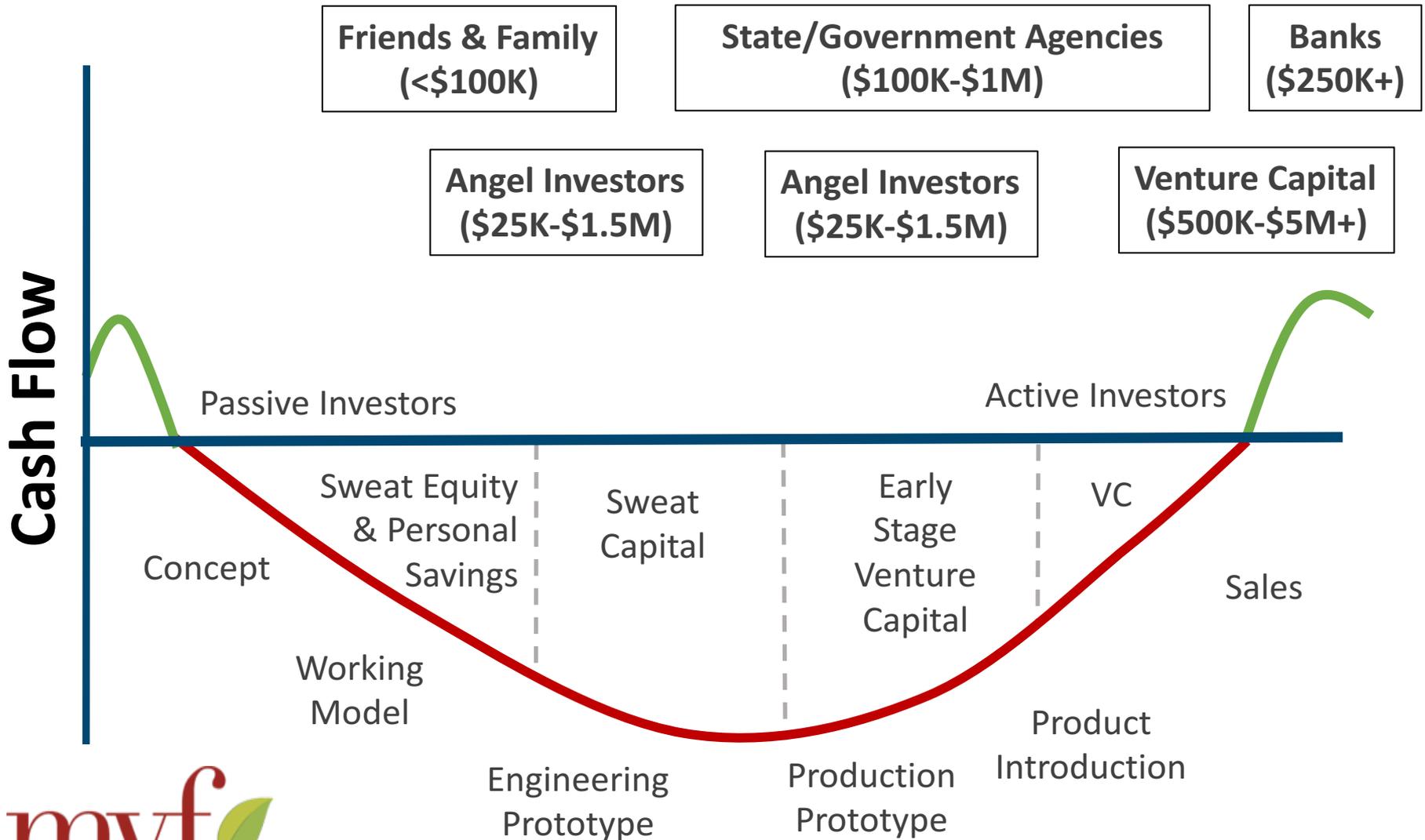
- Accelerators
- Moving to extend sources of seed & seed + funding ... **usually angels**

Every Sector can have a Swarm of Startups

Unbundling FedEx

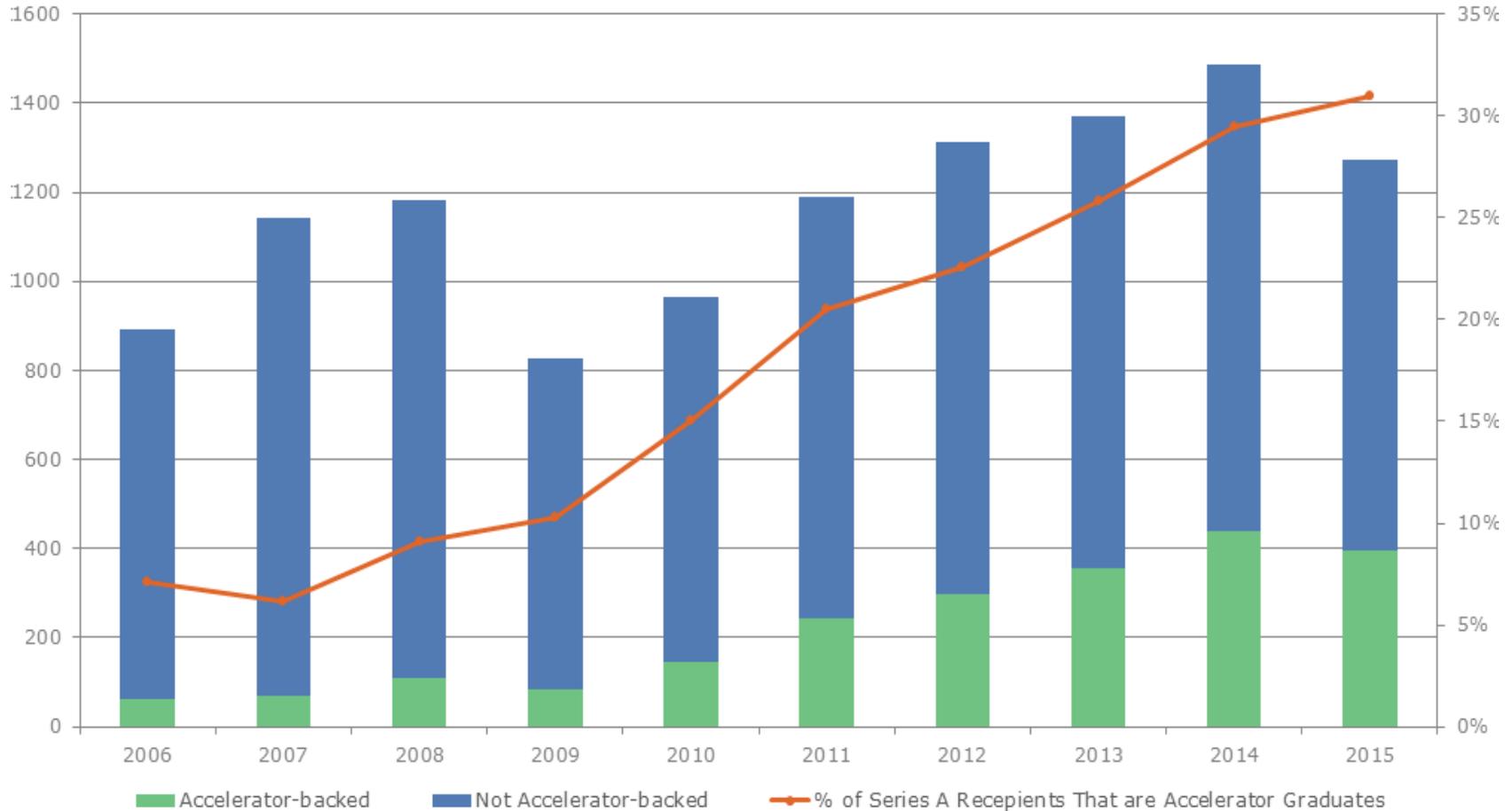


Different Sources of Capital



Accelerators prior to Series A

Breakdown of U.S.-based Startups to Raise a Series A Round



One-third of U.S. startups that raised a Series A in '15 went through an accelerator

Alternative sources of capital

Revenue – best of all (Bootstrapping)

- Pre-payments, etc. from customers, NRE to jointly build product
- Revenue history opens access to more types of debt

Vendors & Partners

- Partner for co-marketing, finders fee, etc.
- Delayed payment for raw materials from suppliers, etc.
- Can lead to other collaborations

Grants

- SBIR (Small Business Innovation Research) grants department-specific funding – usually \$800K in 2 phases (slow)
- \$2.5B set aside from Federal agencies since 1982 ~ \$2 Billion +
- Stimulate technical innovation to meet federal R&D needs
- Principal Investigator (PI) should be employed by small business

Other Foundation & Government Funding

Debt & Venture Debt

All the above can be used by early-stage high-growth companies and by “normal growth” companies

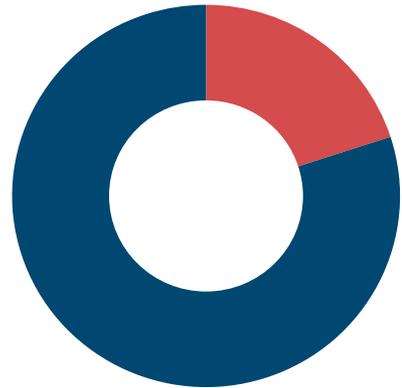
Impact Investing

- All investments have impact
- Impact investments are investments made into companies, organizations with the intention to generate social and impact alongside a financial return
 - Returns can reflect difficulty of the markets served
- The growing impact investment market provides capital to address the world's most pressing challenges in sectors such as sustainable agriculture, renewable energy, conservation, microfinance, and affordable and accessible basic services including housing, healthcare, and education
 - Knowledge of key funders needed
 - Help the companies collect metrics

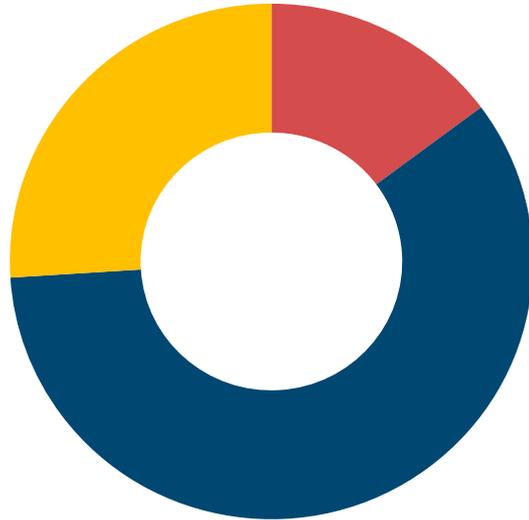
Business Angels vs Venture Capital

	Business Angels	Venture Capital
Who	<ul style="list-style-type: none">• Private individuals• Investing their own money	<ul style="list-style-type: none">• Professional investors• Investing money from others
How	<ul style="list-style-type: none">• Invest 2-10% of personal wealth• \$10-100K per year each• \$50K-1M per round for minority share of a company	<ul style="list-style-type: none">• Invest \$5-20M per investment• Closed period of 8-10 years• Money raised must make more money
Why	<ul style="list-style-type: none">• Make money• Mentor• Socialize• Entrepreneurial track	<ul style="list-style-type: none">• Career• Make money• Raise a new fund

Equity Capital: Goal is Increasing Value



■ Employees ■ Founders



■ Employees ■ Founders ■ Angels



■ Employees ■ Founders ■ VCs ■ Angels

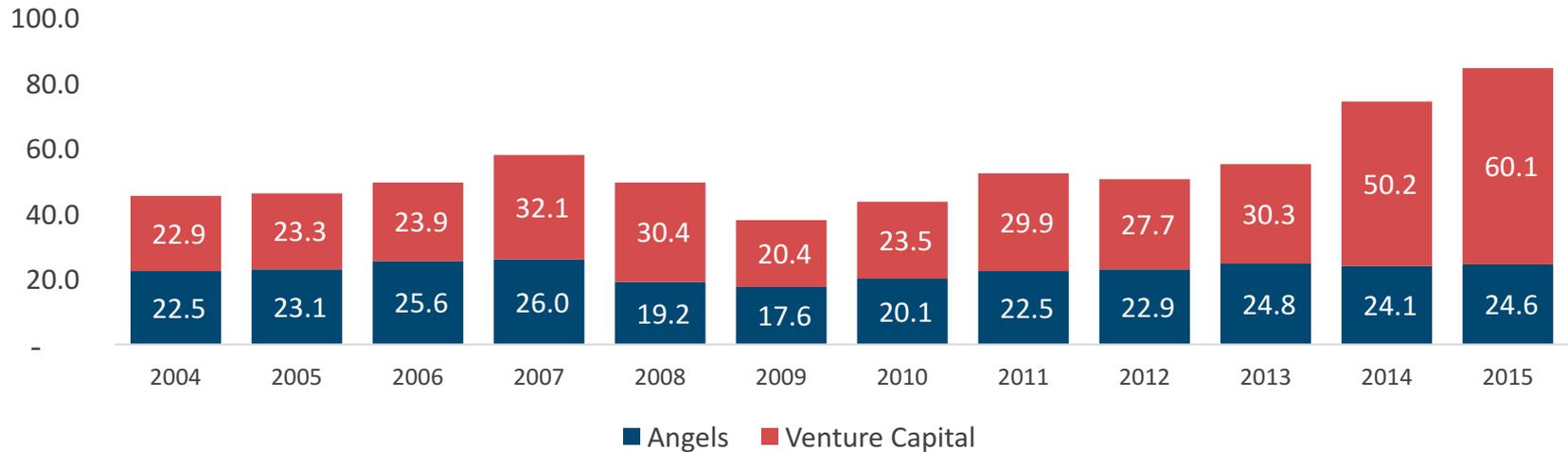
Remember!

- It's the area of the pie slice not the %
- All parties agree ... focus on building value

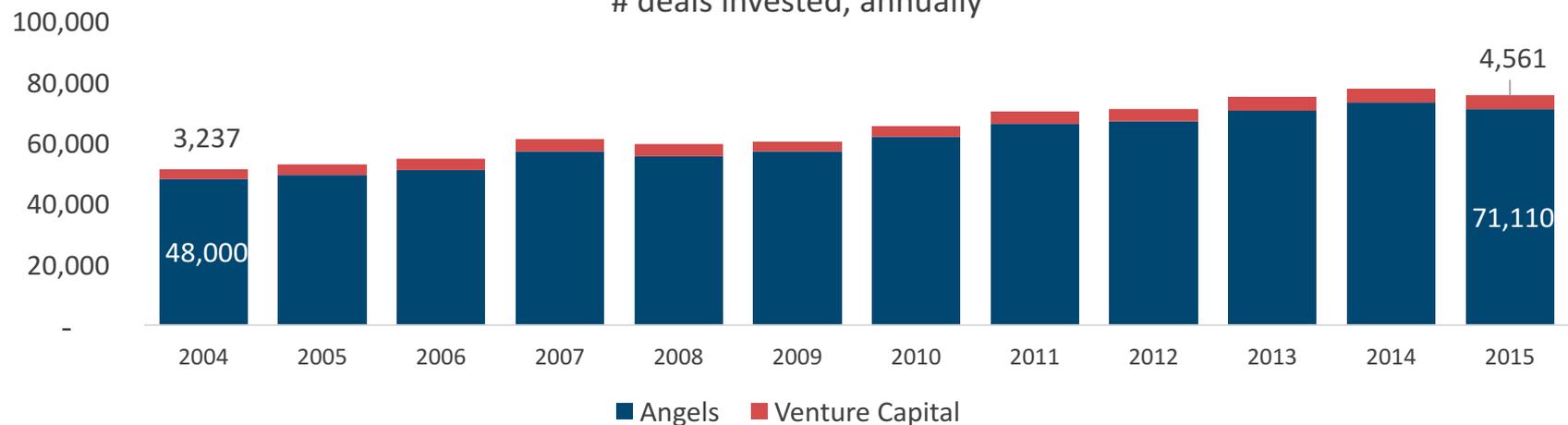
EQUITY REQUIRES AN EXIT

Angels and VC's

\$B invested, annually



deals invested, annually



Angels seed investment: Critical at top of the funnel

Angel Investing

- Angel investing plays the **key** role at the **top of the funding pyramid**
- Complemented by about \$60B VC dollars;
- Estimates are hard but maybe **1/3 to growth** companies and 2/3

Angels

Angels are high net-worth individuals who **invest own money** in start-up companies **in exchange for an equity** share of the businesses

Angel Deals

- 20-40% of angel deals go on to more equity funding (Series A) toward exit
- Most are follow-on angel \$ and some VC; heading to small M&A exit
- Some move to life style companies and a lot fail

Okay, what about me?

- Does this fit?
- Will it fit next year?
- ...How to proceed?

High Risk



- 2-10% of Net Assets (minus primary residence)
- Figure out your budget
- Keep funds for later rounds and upcoming companies



What other training is 'needed'

Core Subject / Concept	Advanced Version
Screening & Community Roles	Management of Angel Group Process
Due Diligence *	Deal Lead, Diligence Process & Syndication Management
Deal Terms *	Deal Structure, Valuations & Cap Tables, Legal Terms
Coaching, Advising, Board Member	Board Member Handbook
Portfolio Review	Portfolio & Exit Management

- **Everyone should understand the basics**
- **Each investing unit needs cover most of these issues**
- **Each person can / should play a role**

Angel Investing

**What investors need to know
about a company to decide**

What type of company is it?

Nature of business

- If you sell software on the internet then,
- You find eyeballs and convert to sales

Type of company

How you bring the product to market

- License new battery technology to existing players VS
- Build a battery company with outsource manufacturing OR
- Build a manufacturer

Cost of scaling and funding requirements

- Every company's financing path is **unique**
- Funding comes in **distinct** flavors; all financial partners are **specialists**

Is this company ready for funding?

Stage of development

Concept

probably friends & family,
maybe an individual angel

Prototype

some angel group interest

First revenue

lots of angel group
interest

Clear capital requirements

Team in place or
identified

In depth financials

Executive summary
& investor pitch

References
& diligence materials



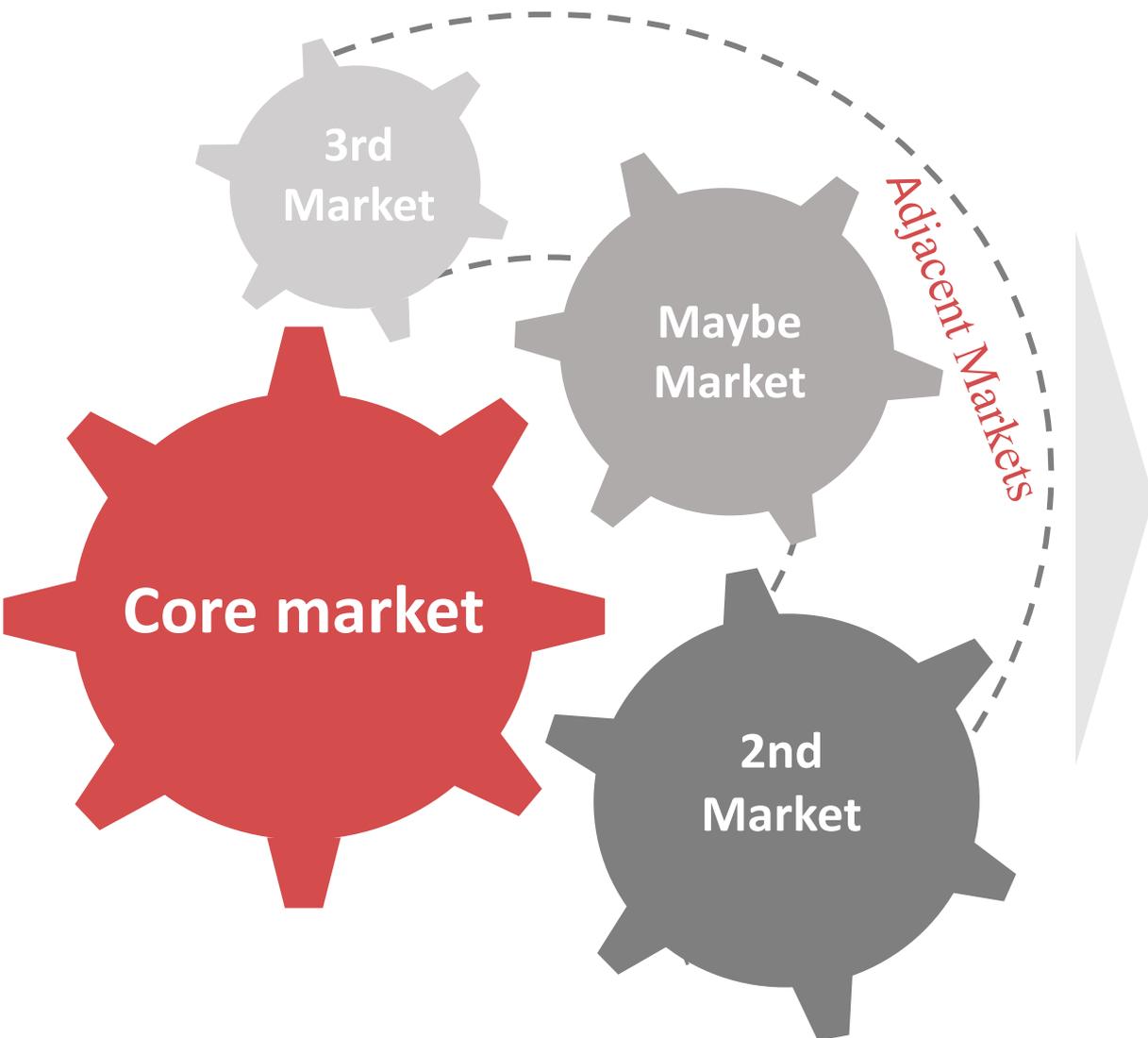
5 P's of investing

PRODUCT	both differentiated technology or service and the market need and size
PROMOTION	market entry plan and cost of marketing
PRODUCT	a business model that has margins and distributions costs that are profitable
PEOPLE	a team to meet the needs of the business
PLAN	good idea of the steps needed to create a repeatable business model

KEY CONCEPTS

- What potential customers are saying
- How to run a series of market entry tests
- How the team matches the needs of the business
- How this will scale against a repeatable business model

Total Market Size: Including Adjacent markets



A look ahead ...

- Core market is compelling
- But there are adjacent markets to explore

Company Risk Assessment

Diligence Factors

Leadership Assessment

Technology, IP & Product Roadmap

Regulatory Strategy

Customer Need & GTM Plan

Uniqueness & Competition

Market Size & Market Opportunity

Financial Projections & Funding Strategy

Exit Strategy

- 1. Risk / Return assessment**
- 2. Match to the human capital and capital available to this deal**

12 Innovation Facts

1. Innovation drives economic growth and raises wages.
2. Innovation improves U.S. life expectancy.
3. Innovation makes technology affordable.
4. New organizational structures lead to rising standards of living.
5. New household technologies allow more time for family and leisure.
6. The pace of American innovation has slowed during the past four decades.
7. Innovation has failed to increase wages for a substantial number of Americans.
8. Significant barriers to innovation exist in the government and the private sector.
9. Federal support for research & development has declined in recent years.
10. Relatively few U.S. college students study fields critical to innovation.
11. American women are less likely to continue in STEM fields than American men.
12. U.S. policy makes it difficult for international students to stay and work.

New England's Angel Association

- Innovation in our region is unique & dynamic
- Angel investing a key part of the funding path

High Risk



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- Figure out your budget
- Keep funds for later rounds and upcoming companies



OK what about me?

- Does this fit?
- Will it fit next year?
- How to proceed?

Q & A
