

Important Things for Entrepreneurs to Know about Angel Investors

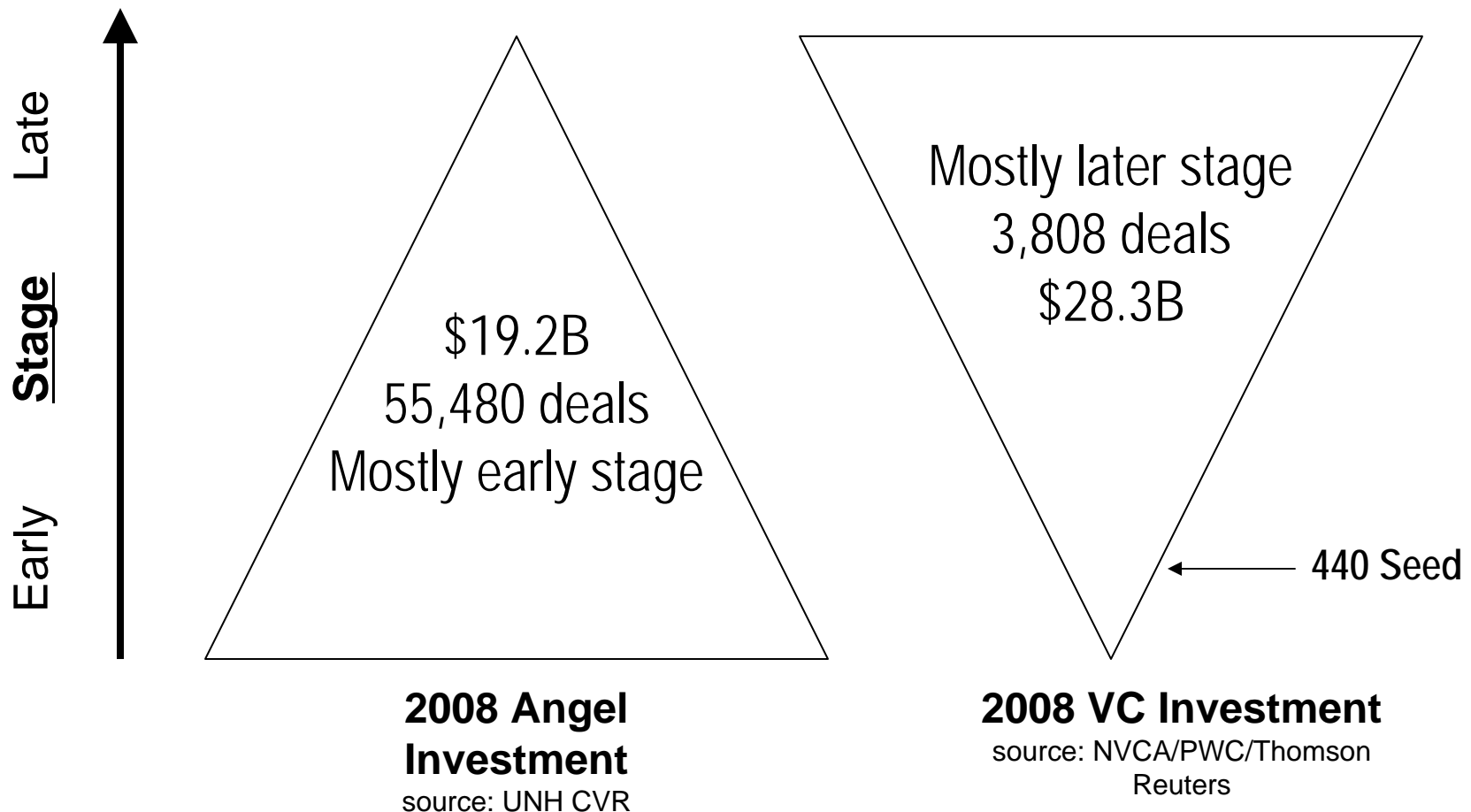
HAIL TO THE JOB CREATORS

From 1980 to 2005,
firms less than five
years old accounted
for all net job growth in
the United States.

*Business Dynamics
Statistics Briefing: Jobs
Created from Business
Start-ups in the United
States, January, 2009.*

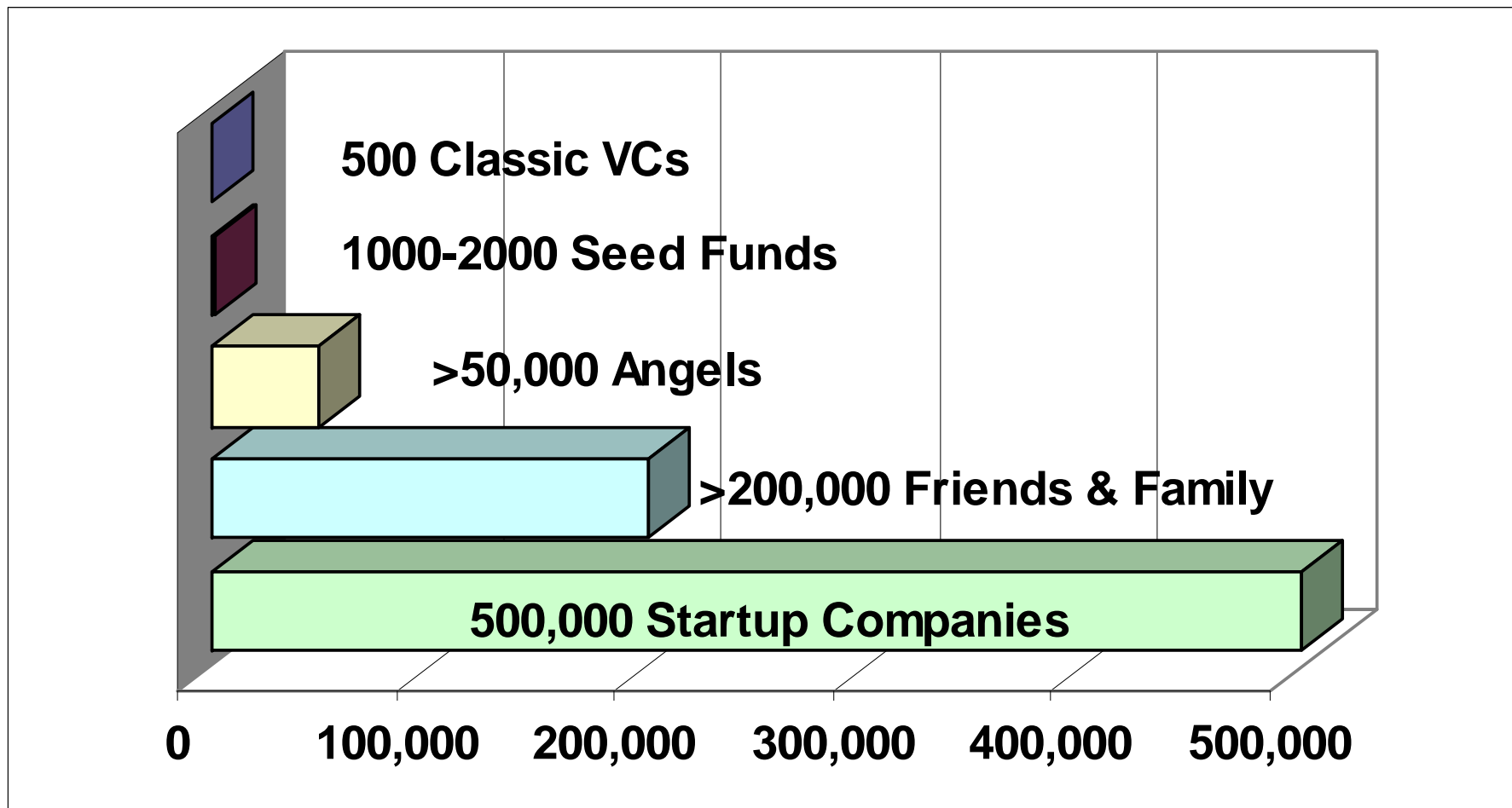


Equity Capital Markets Large, Complementary

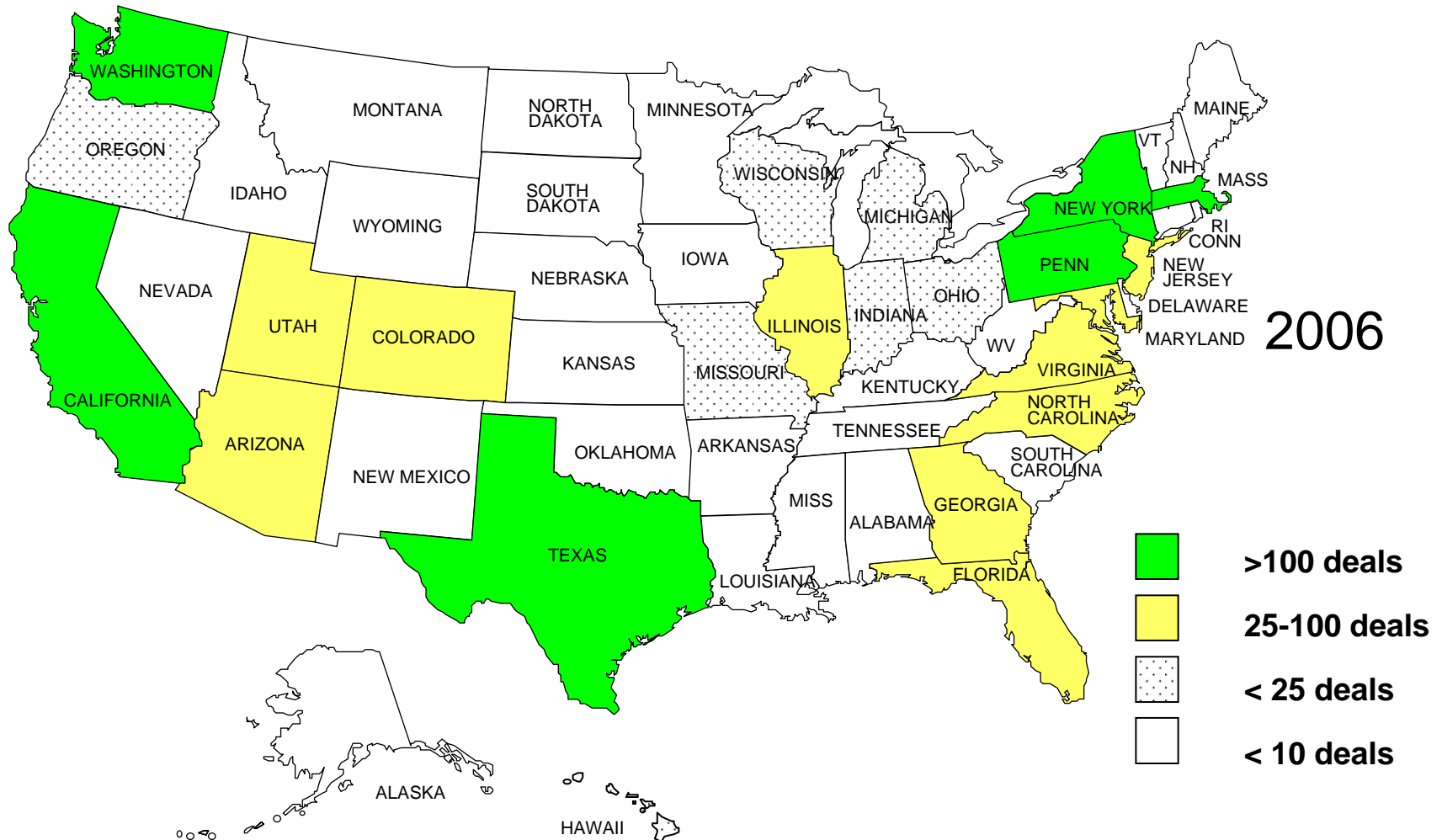


New Company Formation

Source of Equity Funds – Typical Year

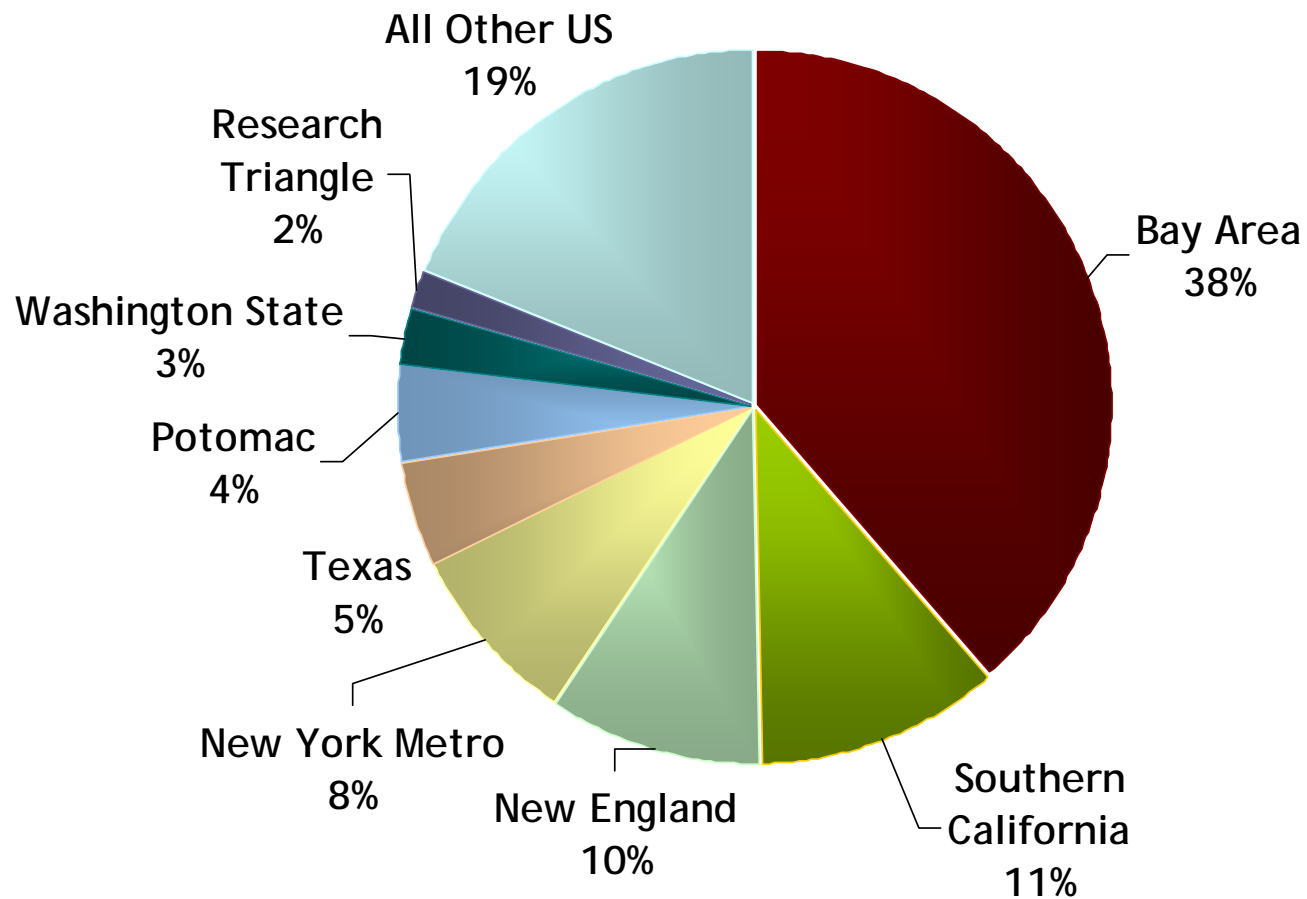


VC Deals by State



Bay Area Draws Most Investment Dollars

Regional Investment in the United States 3Q'06



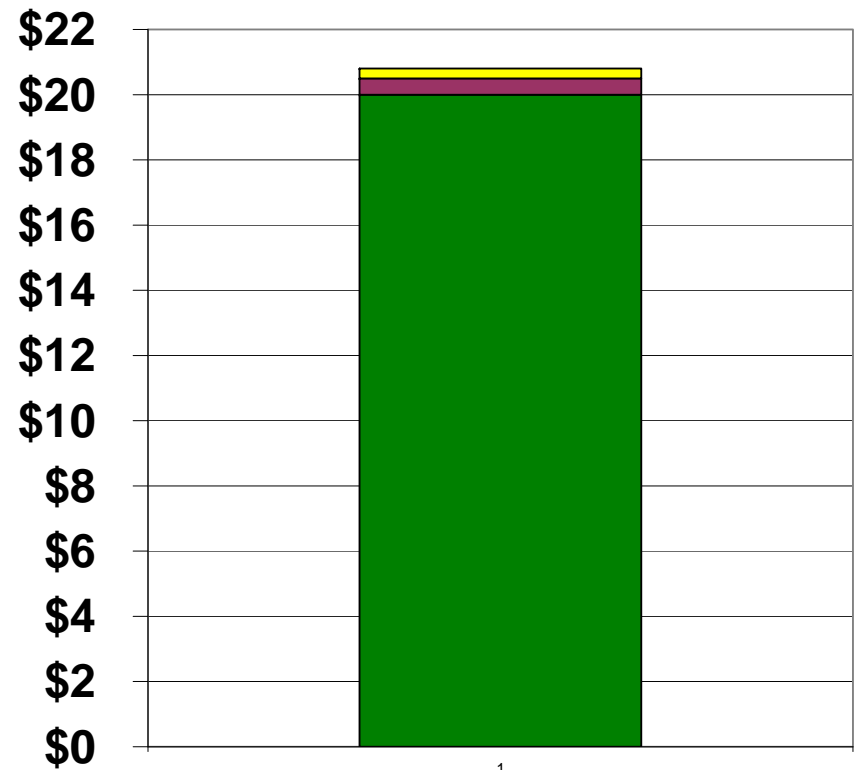
Source: Dow Jones VentureOne/Ernst & Young

Annual Sources of Start-up Funding

Venture Capital ~\$.3 billion
State Funds ~\$.5 billion
Angel Investors ~\$20 billion

Angels: 90% of outside equity for start-ups?

Friends & Family ~\$60 billion



Companies Backed by American Angels



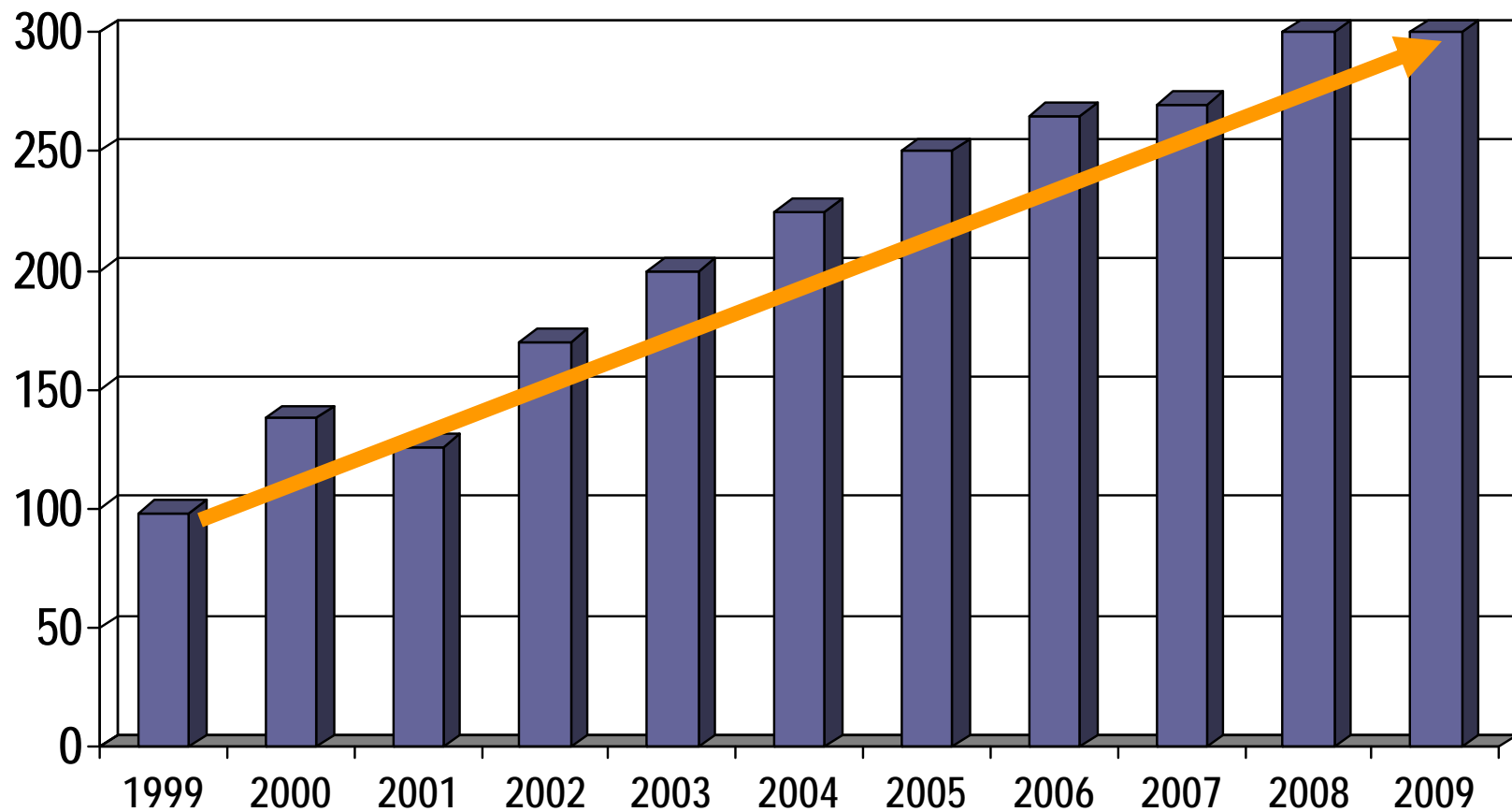
Why Angels Matter

A really great angel helps an entrepreneur:

1. See around the corner
2. Gain a sober second opinion
3. Network with people who can help build the business
4. By being an ambassador
5. Gain credibility in a field

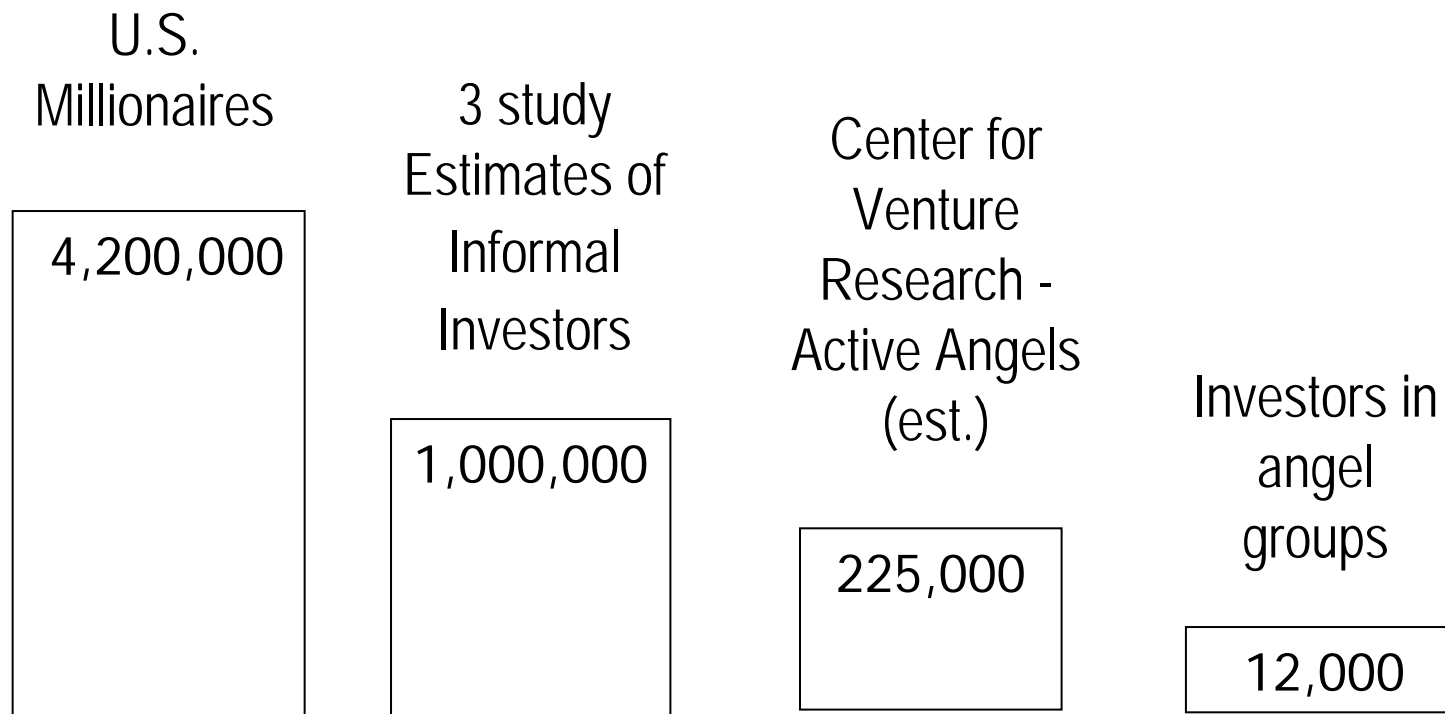
Source: David Pecaut, Boston Consulting Group, 9/06 NAO

Growth in Number of American Angel Groups



Sources: Center for Venture Research (pre 03 data) and Kauffman Foundation/ACEF (04-09 data)

Angel Groups are Small - but Important - Subset of All American Angels



2009 Report from Spectrem: \$1 millionaires down in 2008 27%, those with \$5 million down 28%
World Wealth Report (Capgemini): 19% drop in HNWI and 22.8% drop in wealth in 2008

Premise on Angel Groups

- Creating new class of investor
 - Entrepreneur-friendly
 - Developing sophistication/ excellent processes
 - Growing geographic diversity
- Market efficiencies developing
 - Entrepreneurs can locate more easily
 - Investors get better quality deal flow, while individuals maintain anonymity
 - Building partnerships with other angel groups and VC community for follow-on funding
- Beginning to close capital gap

Angel Organizations Can Help Fill Capital Gap

Stage	Pre-Seed	Seed/Start-Up		Early	Later
Source	Founders, Friends and Family	Individual Angels	Funding Gap between \$500,000 and \$2,000,000/\$5,000,000 (depending on region)	Venture Funds	
Investment	\$25,000 to \$100,000	\$100,000 to \$500,000		\$2,000,000/\$5,000,000 and up	

Comparing Average Group Investment Data

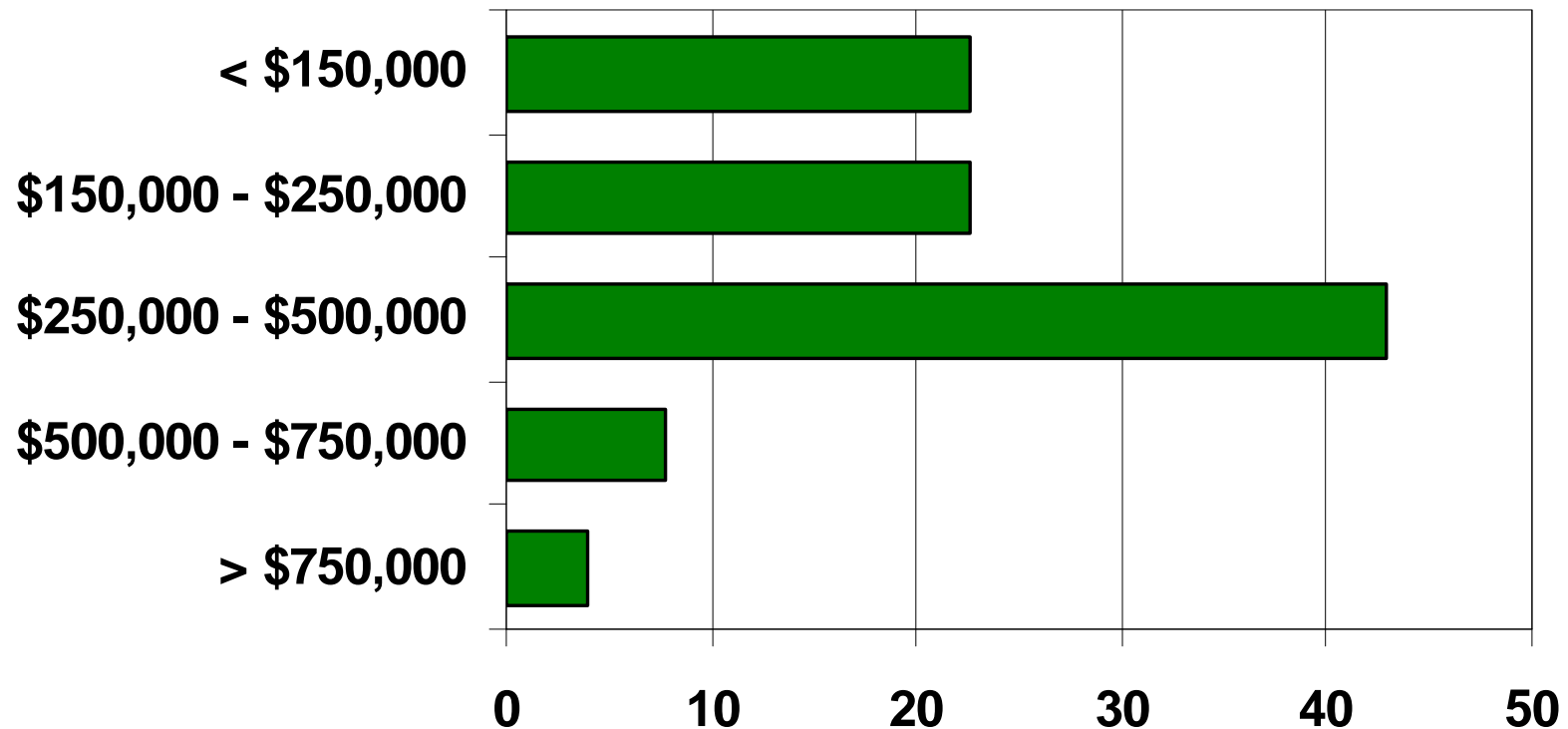
	2008	2007	2006
Number of investments	6.3	7.3	7.4
Total dollars invested	\$1.77 mil	\$1.94 mil	\$1.78 mil
Dollars invested per round	\$276,918	\$265,926	\$241,528
Number of new companies	3.7	4.5	4

In 2008:

- 62.7% had follow-on or co-investments with VC firms
- 23.4% had 1 or more positive exits

Source: ACA Angel Group Confidence Surveys – 2007, 2008, and 2009 (self-reported, not verified)

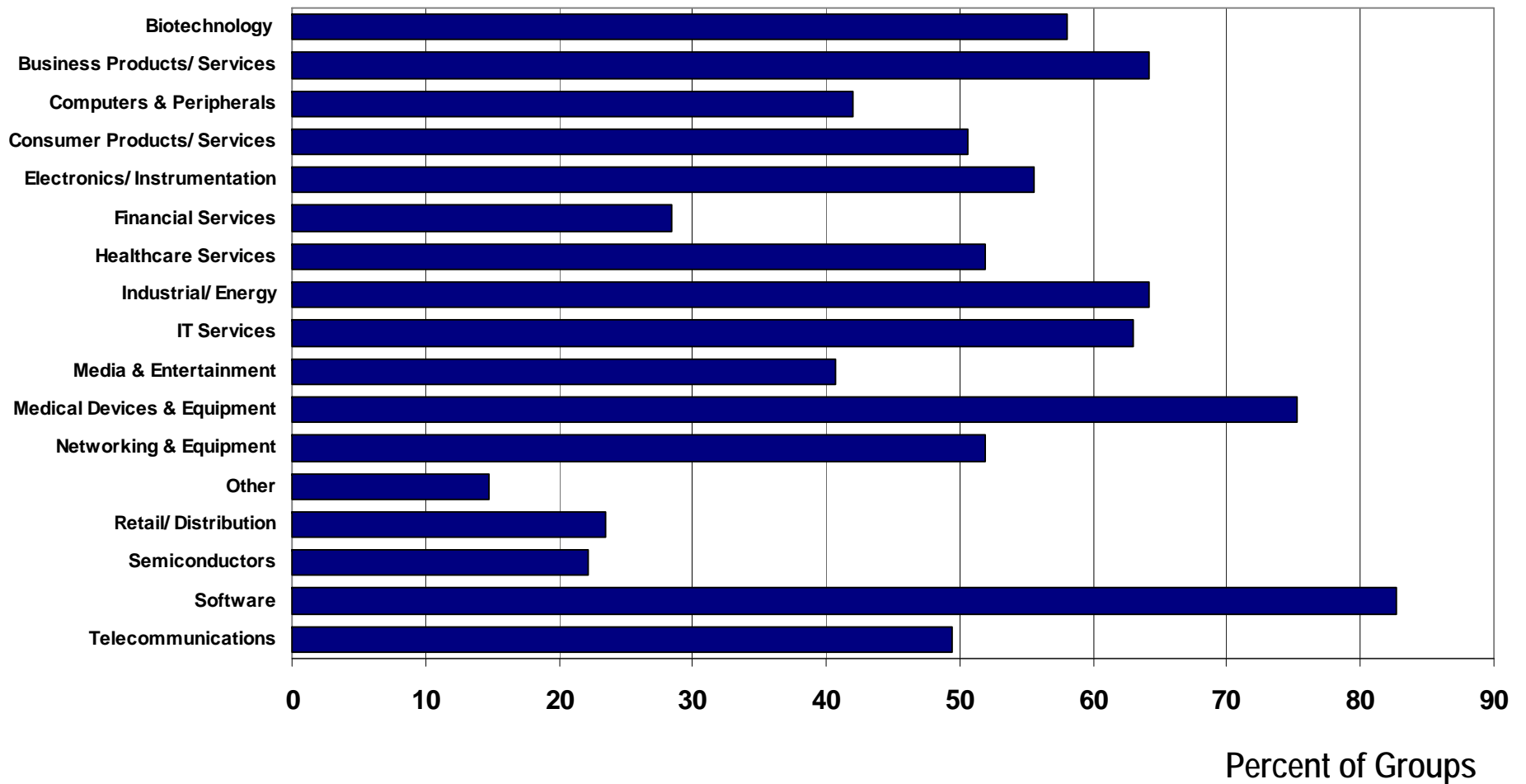
Average Preferred Investment Per Round - 2008



Percent of
Groups

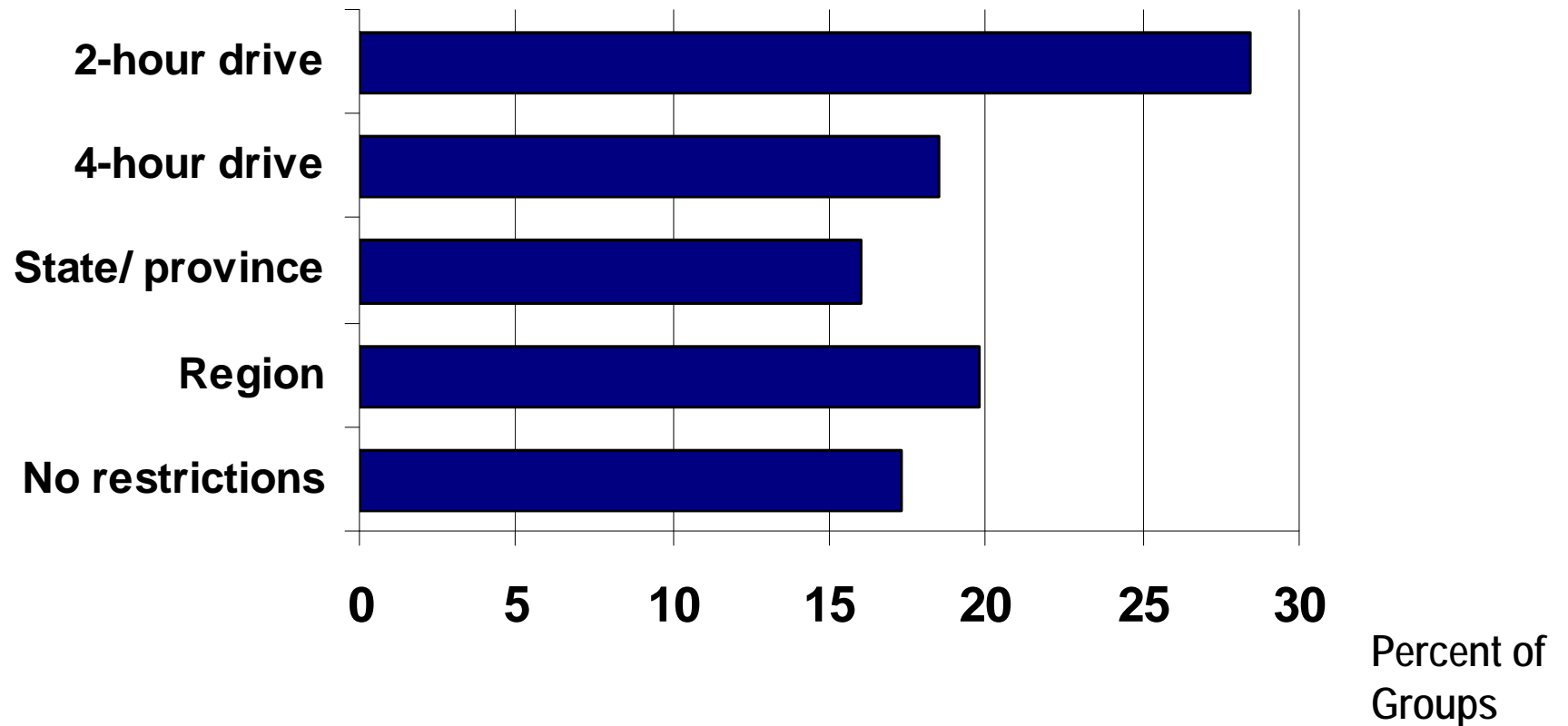
Source: 2009 ACA Angel Group Confidence Survey and 2008 Member Directory

Investment Preference – 2007-2008



Source: 2008 ACA Angel Group Confidence Survey

Geography – Where do Groups Invest?

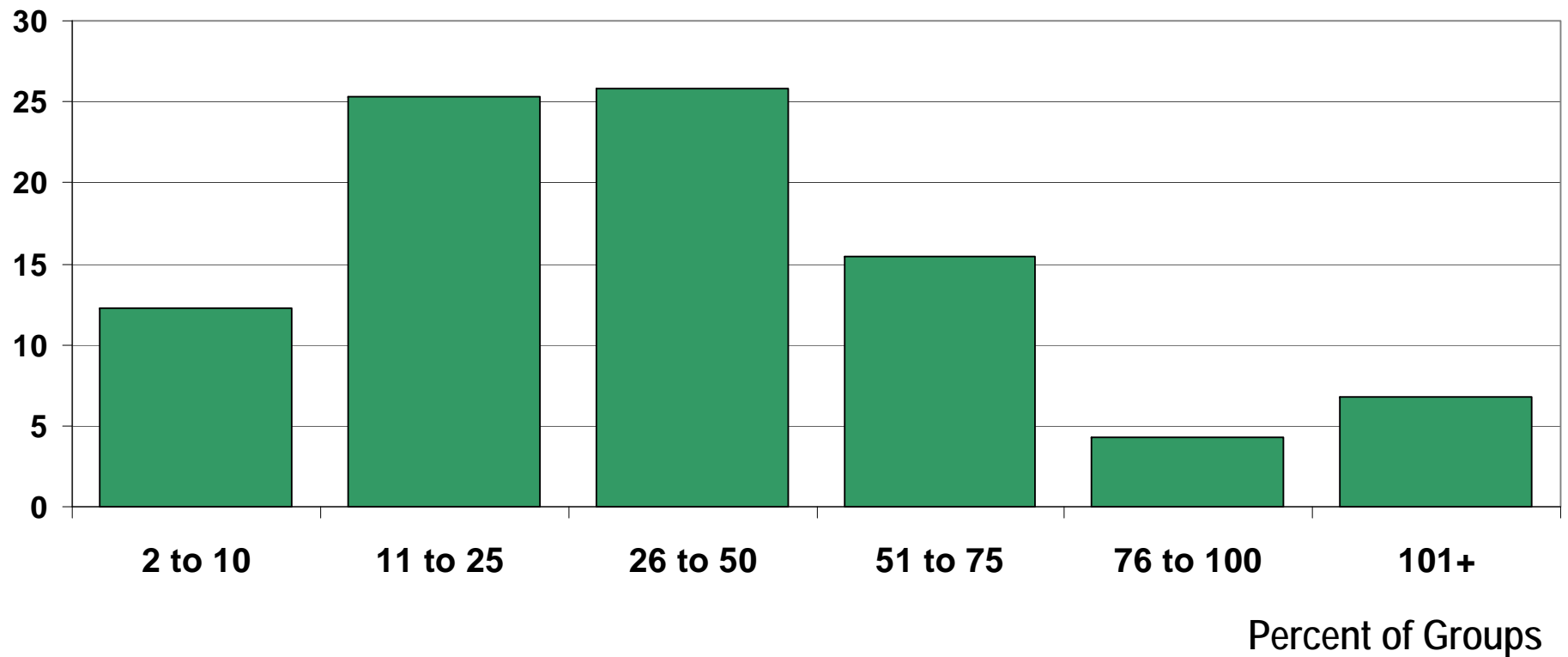


Source: 2008 ACA Angel Group Confidence Survey

Investors Per Group

Average = 43.6

Median = 32.5



Source: 2009 ACA Confidence Survey and 2008 Member Directory

Engaging Angels

- How do you find angels?
- What do angels expect?
- What attracts them to deals and/or entrepreneurs?
- What do entrepreneurs need to provide to angels?

Finding Angels

- Business plan in top shape
- Referral from someone the angel knows and trusts (lots of networking)
- Web site matching – caution!
 - www.vfinance.com, <http://activecapital.org>, www.gensx.com,
www.fundinguniverse.com
- Find local angel group
- Directories of angel groups:
 - U.K: www.bbaa.org/uk
 - Europe: www.eban.org
 - North America: www.angelcapitaleducation.org
 - North America: www.angelcapitalassociation.org (includes only ACA member groups)

Investment Expectations

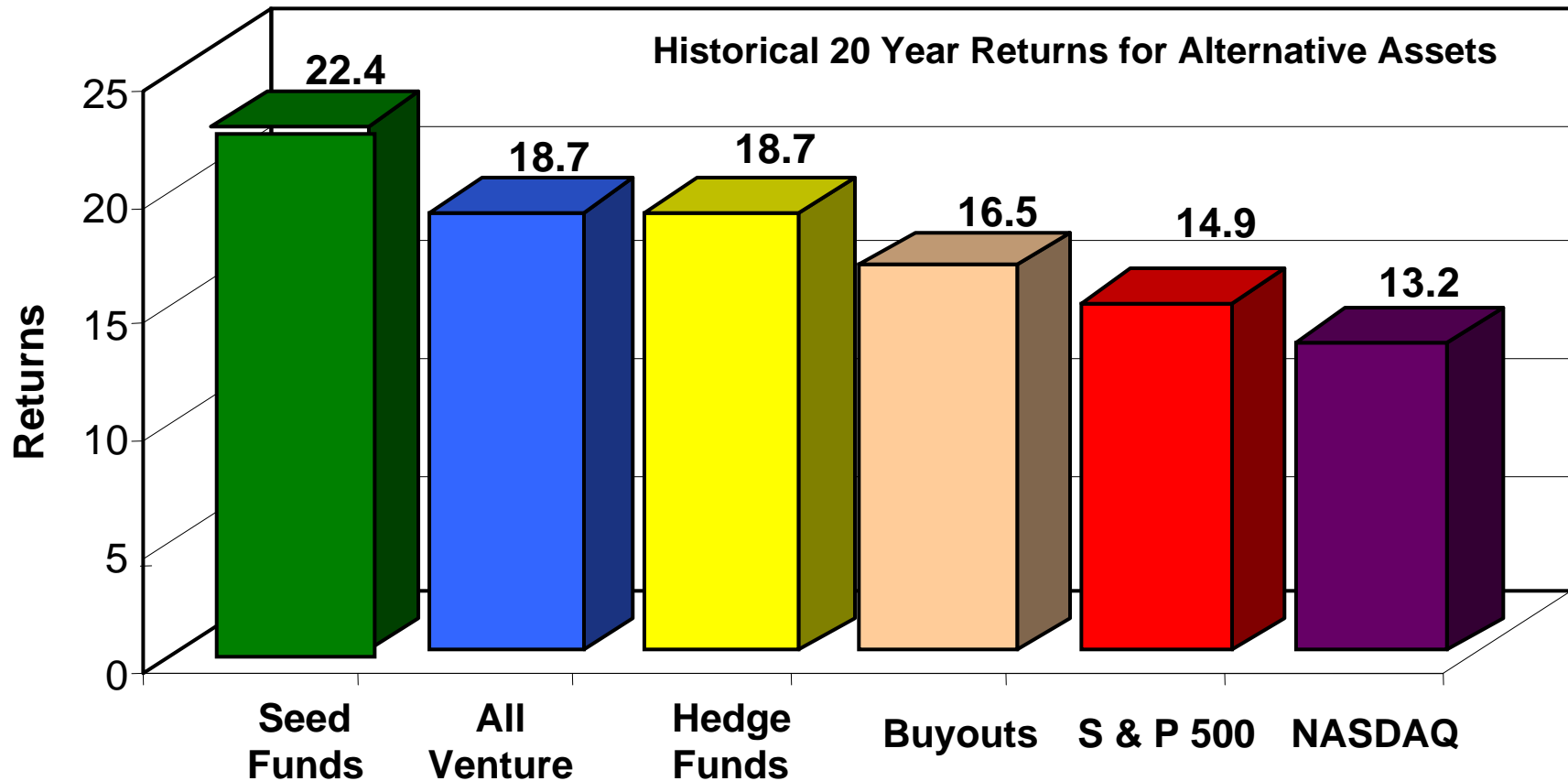
- From investor's perspective
 - Return on Investment
 - Company involvement
 - As advisor
 - On board
 - Part of management
 - Or some want to be passive
- From company's perspective
 - Find or provide follow-on investments
 - Introduction to potential partners or customers
 - Very little interaction

A Word About Return Expectations

- **Angel investing is VERY risky**
 - 1 or 2 of every 10 investments brings most of return
 - Hard to tell which companies will return
- **Current return estimates for portfolios:**
 - Annual IRR of 27% - 2.6X in 3.5 years*
- **If business gets VC funding later, angel investment is often diluted**
- **Some really great angels therefore looking for 10 to 30X potential**
 - Wide variety of expectations, depending on mix of motivations to be an angel
- **Correct valuation is critical**

*Source: Rob Wiltbank, Willamette University, November, 2007 paper

Angel Returns: 20-25% Per Year?



**November study: IRR = 27%
or 2.6X in 3.5 years**

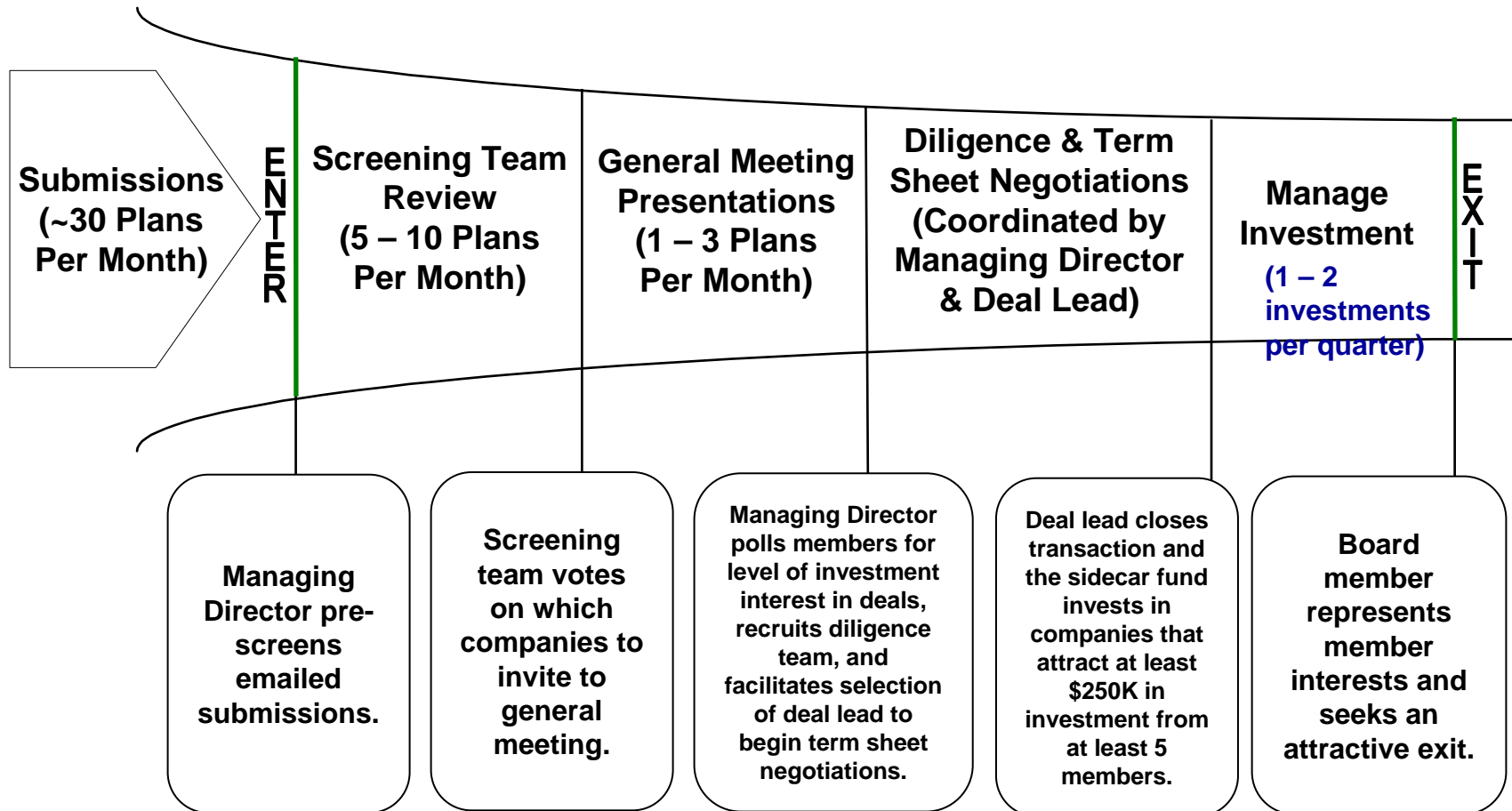
Source: Venture Economics, HFRI Equity Hedge Index

Rob Wiltbank, Willamette University

Process, Deals & Implications

- What's the process for investment?
- What do the deals look like?
- What issues do entrepreneurs need to consider for angel and follow-on funding?

How Angel Groups Work: Typical Deal Process



Source: James Geshwiler, CommonAngels, Boston

Deal Flow Statistics – Angel Groups

- Prescreening 1 in 4 to screening
- Screening 1 in 3 to DD/ present
- Due Diligence 1 in 3 to investment meeting
- Investment 1 in 2 raise money
- OVERALL 1 to 4 in 100 who apply
receive investment

Writing Business Plans

- Entrepreneur MUST write plan (no consultants)
- See Pitching Angel Investors
at www.eVenturing.com (Kauffman site)
- Use editors for clarity and brevity
- Resources:
 - SBA - http://www.sba.gov/starting_business/index.html
 - The Business Mentor - www.fasttrac.org
 - INC Business Plan Building, Section by Section
http://www.inc.com/guides/write_biz_plan/20660.html

Forms of Business Plans

Elevator Pitch	Two minute verbal summary Product, opportunity, differentiation Attract interest – not closing
Executive Summary	2-4 page written summary Balanced presentation Attract interest – not closing
PowerPoint	20 minute verbal presentation Cover whole plan Find serious investors
Full business plan (write full plan first)	20-50 pages plus appendices Validation scorecard (due diligence) Basis for all other plan forms

Angel Rating System

Management Team	0-30%
Size of Opportunity	0-25%
Product or Service	0-10%
Sales Channels	0-10%
Stage of Business	0-10%
Size of this round	0 - 5%
Need for more funding	0 - 5%
Quality of plan	0 - 5%

Fundable Management Teams

- CEO
 - CEO experience
 - Vertical experience
 - Coachable (very important)
 - Leadership
- Team
 - Balance & Complete
 - Experience working together

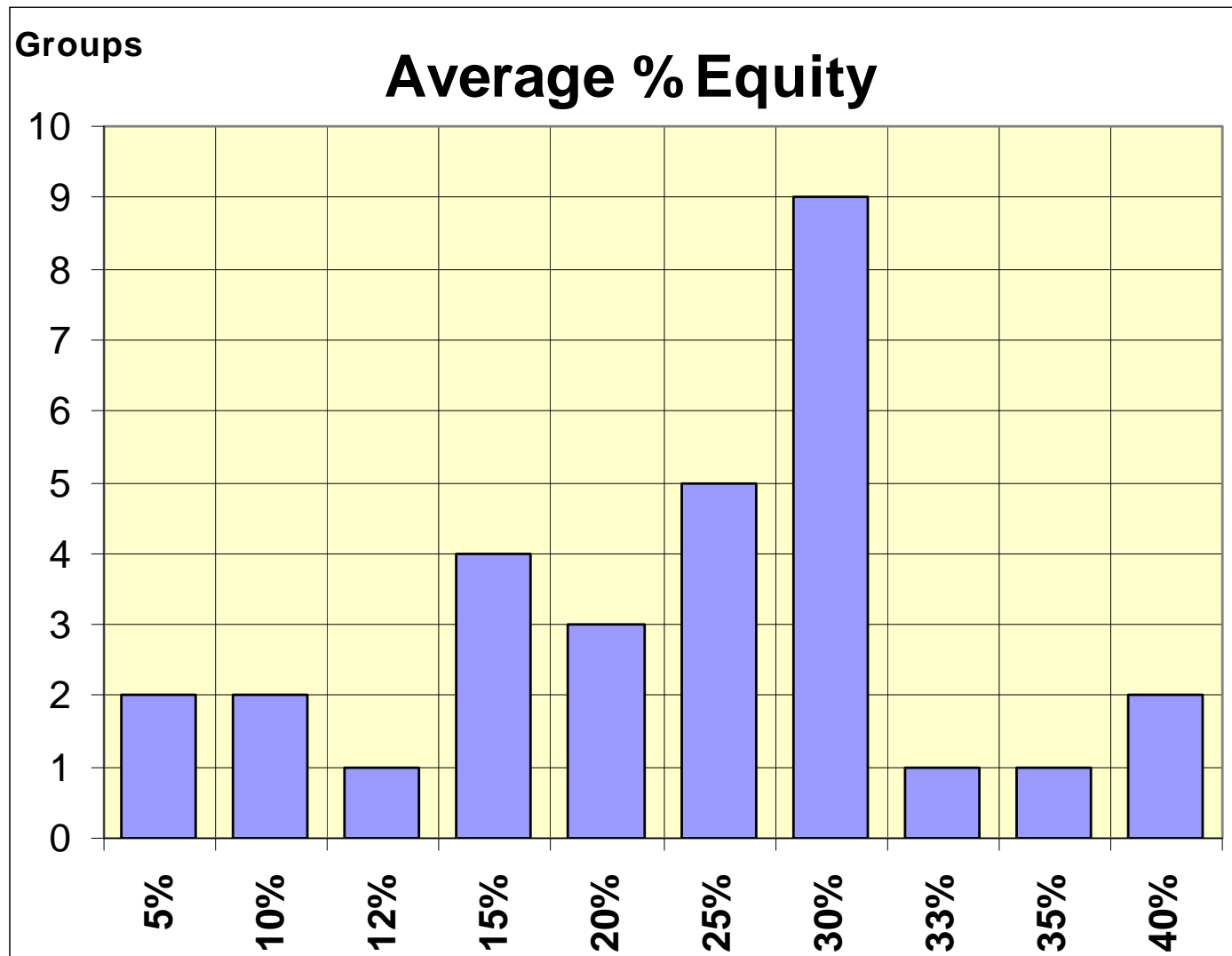
The Opportunity

- Scalable
 - \$30 million (min.) in revenues in 5 years
 - (VCs look for \$100 million)
- High gross margins
- Large niche market
- Unfair competitive advantage
- Ready for customers

Terms Preferred by Sophisticated Angels

Moving toward “vanilla” term sheets with:

- Preferred stock
- Liquidation preference
- Board & information rights
- Anti-dilution
- Participation rights



39 groups reporting (Caution: source data is incomplete & unverified)

Common Mistakes in Pitching Angels

- Only discuss technology/product
- Not prepared for presentation
(practice, practice, practice!)
- Presentation too long
- Inappropriate appearance

Once you get investors to the table...

Closing the Deal

Understand the Process

- Read how angel groups work

*(Cutting-Edge Practices in American Angel Investing
J. May & E. O'Halloran, U of VA)*

- Look on the website of your local group
- Network with those familiar with the process
- Know what to expect
- Be open and honest with investors
- Remain patient

Understand the Terms

- Start-up funding terms are unique
- Study these terms
 - Read *Term Sheets & Valuation* (A. Wilmerding - \$15)
 - Talk to your advisors
 - Consult with experience entrepreneurs
- Stay flexible on terms, especially valuation
- Understand common practice
(your region and business vertical)

Closing

- Read and understand the closing documents
- Remain patient with investors
- Communicate regularly with possible investors, use friendly persuasion
- Pursue low hanging fruit
- Get the deal closed...and **execute the plan!**

Kauffman Foundation's Angel Initiatives

- Education on investment process and opportunity
 - Power of Angel Investing
- Develop data and support research ([Returns study](#))
- Promote best practices and collaboration among angel groups
 - Angel Capital Education Foundation
- Develop tools/ education on starting groups
- Promote role models to expand participation of women and minorities

Information, Resources, and Support

ANGEL CAPITAL ASSOCIATION
THE PROFESSIONAL ALLIANCE OF ANGEL GROUPS

- Kauffman Foundation www.eVenturing.com
- www.angelcapitaleducation.org
- Angel Investor News
- Inc Magazine (and Web site)
- Books (see www.angelcapitaleducation.org)
 - ✓ *Term Sheets & Valuation – A Line by Line Look at the Intricacies of Venture Capital Term Sheets & Valuation*, A. Wilmerding (2003) \$10 from www.amazon.com
- Top level entrepreneurial support orgs
- Web sites match entrepreneurs and investors

Need More Information?

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