



**ANGEL RESOURCE INSTITUTE**

# **Angel Investing: Catalyst for Innovation**

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The list of great companies that angel investors financed and helped build is enormous; brilliant innovations, great companies, jobs galore. Bell, Ford Motors, Apple, and Google: they all had funding from angels. Without the initial angel investment of Mike Markkula in Apple Computer, for example, Apple might have never launched in a meaningful way. His investment, alongside true entrepreneurial dedication, passion, and insight, helped launch a new industry. From group angel investors to ‘super angels’ to investors that straddle the formal VC and angel investing worlds, the relationship between angels and entrepreneurs is vital.

Over the past 15 years these angel investors have become significantly more professional, organized, and easier to “see” by the media following new ventures. Our focus here is to clarify the different types and activities of angel investors, with a detailed focus on a group of extremely active angel investors commonly referred to as “Super Angels.”

Over the last 18 months we’ve interviewed very active angel investors on the west and east coast to explore their views on venture investing. The individuals have invested between \$5 million and \$100 million of their own money directly into between eight and 90 new ventures each (an average of about 30 angel investments per investor). They backed companies like Google, Twitter, A123, Amgen, AutoCAD, Intel, Apple, National Semiconductor, Guidant, and Teledyne when they were barely companies. We asked a series of questions to better understand:

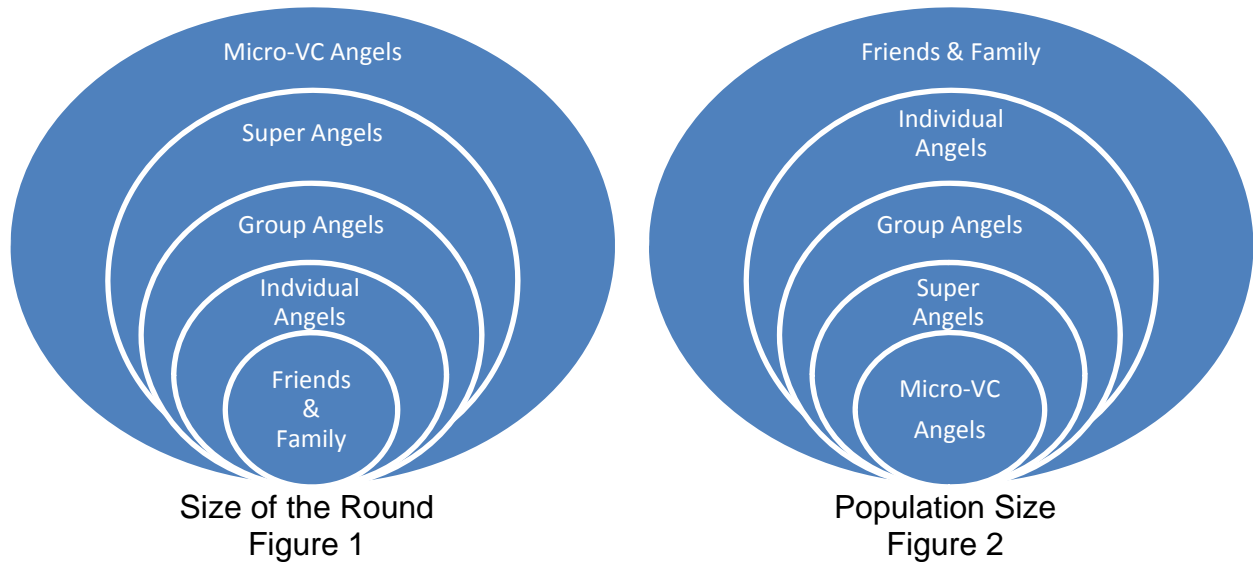
- How vital is their social network to their success?
- Are there any unique patterns in how they select and develop the ventures they back?
- What have they learned about entrepreneurship as a result of their venture investments?

## **Angel Topography**

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We consider angel investors to be people who invest their own capital directly into new ventures. Sometimes they have operational roles in these ventures, but generally they

do not. Sometimes an investment is made into a family member's business, but generally not. Below we propose topography of angel investing to help delineate the difference between types of angels up through formal venture capitalists (VCs). Figure 1 represents the size of the investment round typically done by each type of investor (the larger the area, the larger the round). Figure 2 shows the relative size of the population of each of these groups.



There are exceptions of course, but generally, as one operates in the expanding circles of figure 1, they make larger investments in larger rounds. The friends and family round of financing generally ranges from \$25,000 to \$100,000. At the next stage the entrepreneur often seeks investment from an angel or a few angels – typically this investment ranges from \$50,000 to \$200,000. As angel groups have grown and become more visible, many entrepreneurs approach a group of angels that review investments together, hoping to have them team up to invest in a round from about \$250,000 to \$2 million. Beyond organized angel groups the water gets muddy. Terms such as “Super Angel”, “Micro-VC”, and “Super Angel Funds” get intermingled and can be confusing.

### **Super Angels**

Angel investors who have the capacity to invest large sums of their own money (in excess of several hundred thousand dollars U.S. per year, year after year) we term “Super Angels.” However, some of these individuals attract capital from others and blend their own money into what amounts to a “Micro-VC Fund.” However, they are typically not a traditional VC in that their own money is a significant portion, if not the majority of the fund. By contrast, a VC typically invests others’ money, alongside a relatively small portion of their own money.

Commonly, when one mentions Super Angels, thoughts lead to high-tech investors from Silicon Valley. However, Super Angels are found throughout the country; and not just doing high-tech. We interviewed Super Angels from the East Coast, Northwest,

Southwest, and Silicon Valley. What we found were serial investors who make large angel investments year after year. They are persistent and deliberate in their investing process. They invest in technology ventures but also in other areas. Most all of these super angels have built companies themselves, which is typically what produced the original capital for investment.

A few key differences between these Super Angels and general angel investors in groups became apparent: the speed with which they invest, the personal network they leverage, and the amount of money they can invest. Some super angels we interviewed had invested more than \$10 million into one company. This capacity allows them to be very patient and work with uniquely capital inefficient companies all of the way to an exit. In addition, when investing, they regularly brought others into the investment with them, and could do so quite quickly. Subsequent to investing, their network and access to companies and talented entrepreneurs was occasionally an advantage, depending on their specific strategy.

As uniquely active investors, and with a capacity to support a company further along their growth, Super Angels, like reputable VCs, are able to attract great deal flow in the areas in which they operate. Often other angel investors follow their lead, participating in rather large angel investment rounds; opportunities that in the past some early stage VCs would normally have done alone. In many ways they are like VCs in that they have rich personal networks providing relatively easy access to VCs, key management talent, strategic partners, and potential acquirers.

## **Super Angels: A Closer Look**

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In our interviews, we focused on three main areas of inquiry of Super Angels. First, what is their approach to early-stage investing? For instance, what criteria, strategy, process, or “rules” do they employ? Second, what role does their network play in their investing? Lastly, what have they learned over their years of investing?

While our research is ongoing, there are some common patterns that jump out thus far.

1. The use of personal resources supports a broad array of successful strategies.
2. Industry *really* matters; this is particularly true in Silicon Valley.
3. The entrepreneur really matters, not just their expertise: No Quitters, No Liars, No Jerks.

We observed a great variety of strategies among these investors. Each of them was a successful entrepreneur in their own right, and had clear ideas about how they believe the ‘game’ is played most effectively. We surmise that the lack of a fund structure, other people’s money, or explicit time horizons supports this variety of strategies. We’ll describe just a few strategies that were particularly coherent.

### ***Broad and Thin***

One strategy we came upon was a strategy of “Broad and Thin”. This strategy utilized investing in many ventures, rarely making follow on investments. The exception to this strategy was when there appeared to be a “no brainer” follow-on investment, generally in which a company was exploding in growth and appeared well on the way to success. These investors did not provide extensive hands-on involvement; however they did provide important support in key moments with regards to penetrating major accounts, introductions to strategic partners, or connections to key money sources such as VCs. In addition, helping the entrepreneur attract the right talent for the management team was in lieu of hands-on involvement that other strategies may have employed.

### ***Co-Founding***

Another strategy was to actually start the venture with 100 percent ownership. We term this “Co-founding” due to the fact that these super angels were actively involved in team formation, paying the bills, stock allocation among partners, and activities at the core of founding a venture. This was similar to a serial entrepreneur’s approach, with the twist that they were only intending to launch rather than directly manage the growth over time. These investors didn’t view their investment as a stock purchase at a valuation, but rather that they owned the firm and used the allocation of stock throughout the team to get things going from the start. This approach allowed the investors to provide specific direction for the firm from launch.

### ***Deep Dive***

Lastly, we found Super Angels who had very deep sector expertise and believed that success was best attained by employing a laser focus on a specific sector. These Super Angels were able to leverage a deep network in a specific industry for management talent, strategic partners, customers, and potential acquirers. This approach often utilized a deep funding commitment and avoiding co-investors entirely until later funding stages. This approach avoided misalignment of investor expertise which often allowed a more effective and smooth growth and strategic alignment. In addition, their network of experts were often very deep since they stay focused in one sector and thus would interact with their network more often and from deeper ties.

### **Industry Focus**

While not all Super Angels invest a lot of capital into one company – it ranged from \$50,000 to \$10 million – they showed a rather extreme commitment to invest within a particular sector. The pace of their investments benefited from the learning and information the investors held within a particular area of expertise. One of the investors was very explicit on this front: “In this sector, if I believe this is a breakthrough opportunity, it is. I have been operating in this space for 30 years.” Their ability to comfortably invest large sums of money into new ventures was directly related to this expertise.

Sector expertise is really specific for these investors. “Medical Devices” does not equal Life Sciences. Software isn’t software – it is business systems, back office, sales support, gaming, etc. Internet isn’t a sector. Generally speaking, their focus was clear along the dimensions of technology or customer type.

This is particularly true of Silicon Valley based Super Angels. Every one of the investors we spoke to that operated in the Silicon Valley area had a narrow focus. Outside of Silicon Valley this is significantly less common. While it is speculation, this may largely be due to the presence of fewer deals in any one particular sector in most parts of the country.

### **What They Have Learned**

Lastly, we asked every investor what they have learned from their investments, and what things they wish they knew earlier. Without prompting, and without hesitation, every single investor stated that they were much better at reading people and understanding the risks and potential that the individuals and team dynamics bring to the mix. This went well beyond expertise, or any particular technical aspect of the entrepreneurs; it was much more personal. In part, these things matter because none of these investors need to work; they enjoy the process in addition to any particular financial outcome. As a result, generally speaking, why work with people you don’t enjoy? Their position on people was quite common: big passion required, and absolutely “no quitters, no liars, no jerks.”

A common theme for the super angels was finding people who were deeply passionate about their venture. They were seeking entrepreneurs whose life revolved around the venture idea. Some described this as a level of stubbornness or single-mindedness to the cause. Another stated he looked for entrepreneurs who were the perfect person to build this company because their experience and life revolved around this specific idea. This passion sustained the entrepreneurs to stay the course - thus their passion was intermingled with “no quitters.” As many angels know, building a venture is hard work that requires a rock solid commitment to weather difficult challenges and struggles. The importance of identifying and avoiding quitters was essential in their investing. A key way that they identified passion and commitment was by looking for a clear “fit” between the venture and the entrepreneur.

Additionally, Super Angels wanted to work with entrepreneurs who were honest and reasonable, i.e. no liars, no jerks. Early-stage investors of all kinds know they are likely to have a long term relationship with the entrepreneur (a few years at minimum) and would rather work with people they enjoy than those who may be bright but difficult. When they worried about honesty or integrity, they didn’t invest.

One topic on which they were split is “coachability.” In many cases the investors found this to be vital, a part of their ability to actively guide the venture, with a passionate and committed entrepreneur who was sincerely influenced by their feedback and suggestions. However, a few of the investors we interviewed were unconcerned about how coachable an entrepreneur was, often regarding their expertise and involvement as

nowhere near as critical to the success of the venture as finding the right team and following their lead.

As we mentioned earlier, this research is ongoing. We are still evaluating the different ways their social networks influence their investing, the specific decision rules, and practices for involvement after the investment. Stay tuned.

## **Implications for Angel Groups**

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Angel groups should understand how they can work with super angels in and around their groups. Super angels will likely impact the expectations of entrepreneurs in such a way that angel groups that move slowly may have a harder time attracting the better deals. Creating a collaborative network that can process investment decisions more quickly will be quite valuable. Involved in this process is the issue of group think, and how groups make decisions. Super angels have the luxury of decisiveness and instinct that overly formal groups may inadvertently lose. Another growing aspect of group investing is sidecar funds, funds that invest alongside an active group of angels, which explicitly increase the investment size and activity levels of groups. Like speed improvements, these sidecar funds may become more central to keeping a group relevant to great entrepreneurs, particularly in localities where super angels are active.

We are not suggesting that Super Angels will force all angel groups to change. However, it is likely that in areas where there is a high concentration of angels, super angels, and VCs, competitive pressure will likely push things toward speed and angel fund innovations.

## **Takeaways**

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In summary, our work thus far suggests the following issues to keep in mind:

- A. There is no golden rule that leads to success. Many different strategies, well executed and related to the specific investor, are perfectly workable. Stop looking for the silver bullet.
- B. An entrepreneur's strategy and an angel's strategy actually matter to each other. If you have fundamental differences in how you want to approach the future of a business, it can be a problem. Discover this sooner rather than later.
- C. Because of their sector focus, prior investments by Super Angels are a good indicator of where they may or may not invest in the future. If you are an entrepreneur, look for angels that have made investments in your space already.
- D. An entrepreneur's personal "fit" with an angel investor matters. Note to investors: they know their fit with the entrepreneur matters and will be on their "first date" behavior. Real character is often determined in the reference check Super Angels perform informally within their extensive networks.

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## About the Authors

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## About the Angel Resource Institute

The Angel Resource Institute (ARI) is a charitable organization devoted to increasing the effectiveness and availability of financial and mentor capital to entrepreneurs. We provide education, training, and information on best practices related to the earliest stages of angel investing and new venture development. Through our core competencies of research, data collection and analysis ARI develops educational workshops, white papers, and toolkits for angel investors, entrepreneurs, and the entire startup community.

The founders of the Angel Resource Institute included leading angel investors and entrepreneurs in collaboration with the [Ewing Marion Kauffman Foundation](#). Since becoming an independent organization in 2007 ARI has presented its programs in 34 U.S. states and in 9 other countries. More information is available at [www.angelresourceinstitute.org](http://www.angelresourceinstitute.org).