



Newsletter

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Denise Coleman
Paul Quadros

Membership Committee
Mike Bateman
David Burwen
Brian Frenzel
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Dinner Details

Date: Wed., Sept. 17th, 2008

Place: Los Altos Golf and Country Club

Time: 6:15 - 9:00 pm

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Introduction

Individual angels, or an angel group such as ours, could elect to pursue many different investing strategies. We could try to “draft” behind VCs as passive investors, letting them be the lead and do the hard work of diligence, term structuring, and mentoring on the board. We could syndicate our rounds to VCs, investing \$500k and then looking for VCs to provide the balance of a \$2M round with us acting as the lead. Or we could look for smaller financings that we could do all on our own, as the lead investor of unaffiliated angels or other angel groups. This last category is what we have been increasingly and deliberately targeting at the Band. This strategy has consequences for the kind of deal that succeeds in our screening process. All other things being equal, it is unlikely these days that a deal looking for \$2M at a \$5M pre-money valuation will get invited to present; but one looking for \$500k at \$1.5M pre-money will. Of course, the company needs to be able to “achieve something” with the \$500k to \$1M we can pull together without VC co-investors, so this criteria excludes a lot of potential deals. However, we perceived anecdotally that deals with modest capital requirements and valuations have better outcomes for our angels; and now, we are interested to learn, that an academic study backs up this perception.

Thanks to our member Don Jones for highlighting the study from the School of Business, University of Maryland, College Park. To paraphrase their abstract, authors (Brent Goldfarb, Gerard Hoberg, David Kirsch, Alexander Triantis) examined the impact of business angels on 182 Series A financings and subsequent company outcomes. They found that when only angels participate in a financing round and VCs are absent, the companies are less likely to fail and are more likely to have a successful liquidity event. Not surprisingly control rights are more entrepreneur-friendly, legal expenses are lower, and investors are more geographically proximate to the company. Similarly, when companies were financed exclusively by VC investors they also performed well, particularly when the deals were large. But, companies financed by both angels and VCs experienced inferior outcomes! The authors conclude that:

“business angels are the preferred investors and VCs trying to compete by investing in small deals face adverse selection. For larger deals, where deeper-pocket VC participation is required, these roles reverse and angels face adverse selection when investing alongside powerful VC syndicates.”

I have a copy of this paper if anyone is interested in its full, 42 page, analysis.

In the interests of supporting additional academic work in the area of angel investing I’d like to highlight for you a request made by Christoph Garbotz from Aachen University. Stanford University has set up a research project with Aachen to analyze angel investors’ contact networks, co-investment strategy, and their ‘value added’ to startups. Questions addressed in the research are: How important is the personal contact network of informal investors? What are the most important resources investors can offer to startups? What are the most successful resource combinations in co-investments? Are there major differences in the surveyed countries?