Angel investors tell entrepreneurs how to seek equity capital

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Is your startup company looking for early-stage investment capital? Earlier this month, a Seattle-area group of investors described what they look for in business deals. Investors from the Alliance of Angels shared their views with more than 100 local business owners and entrepreneurs at a forum in Pasco. Alliance members also heard pitches from four pre-screened local companies seeking funding. Local investors were encouraged to consider emerging tech companies and become more involved with peer organizations such as the Alliance.

In the business world, the term angels refers to high-net-worth individuals who invest their own money to help promising young companies get started. Angel investors are betting that the companies in which they take equity will eventually generate a healthy return on that investment. Angels often get personally involved to help companies succeed, offering business mentoring and access to influential industry leaders.

Only a small percentage of companies seeking investment funding actually receive it. The Alliance of Angels has received 600 business plans for review since 1998. Members have invested about $7.8 million total in about 5 percent of those.

Companies can increase their chances of getting funding, Alliance representatives said, by knowing what investors look for and positioning themselves accordingly. Angels speaking at the forum in Pasco shared the following tips.

Understand the decision process.

At the Alliance of Angels, inquiries are screened so that the most promising rise to the top for further consideration. Business plans that meet the Alliance criteria are placed on a members-only Web site for review. Of those, a select few firms are invited to give a 12-minute, face-to-face pitch to the entire Alliance. On average, one in three presenting companies receives funding. Angels do their own due diligence on companies in which they are interested, including checking out the management team's history and calling potential customers. Alliance members decide individually whether to invest, sometimes partnering with colleagues.

Understand the investment criteria.

Each investor group has its own criteria, keyed to its mission and objectives. The Alliance of Angels, for example, funds only early-stage technology companies headquartered in the Northwest. Many of the companies they hear from are in the Internet or telecommunications business. However, Alliance members are looking for a wide variety of technology investments.

Most presenting companies are seeking $500,000 to $3 million. Angels typically expect a 40 percent internal rate of return on their investments. They are more interested in the potential markets and profits than the novelty or features of the product or service.

Do your homework to create a top-notch business plan.

The business plan is the company's most important calling card when seeking funding. The plan should clearly and succinctly describe the product or service being offered. It should describe the management team's expertise and experience, including that of advisory board members.

Competition and marketing issues are the two weakest areas in most business plans and presentations, Alliance members said. An innovative technology does not guarantee customers. Entrepreneurs should describe how the new offering will take market share away from direct and indirect competitors, and how the product will reach potential customers. Financials should include the revenue model, pro forma financial highlights and growth potential.

Get personal.

Because investors are deluged with inquiries, it often takes a personal connection to get their attention. Investors know each other and talk frequently about opportunities and companies that are being shopped around the region.

Angels often require a reference from another investor, or other trusted person, before they will consider an opportunity. They tend to invest in concepts in which they have personal expertise or knowledge.

Once entrepreneurs have fine-tuned their business concept with the help of objective business advisors, they should cultivate relationships in the investment community by attending local and regional networking events.

Present strategically.

Companies that are selected to present should prepare and rehearse extensively, using a diverse, neutral audience as a sounding board. The company CEO should give the presentation, using an electronic Power Point-type format, not viewgraphs. Presenters must stick to the outline and time limit specified by the investor group. Along with an interesting business idea, angels are looking for CEOs who convey their business expertise, passion, commitment and willingness to accept advice.

Give to get.

To get an investor's attention, entrepreneurs should be prepared to give up 25 to 35 percent equity ownership in the first round of funding, Alliance members said. The second round of funding typically involves the same range of equity.

Some entrepreneurs may balk at giving away this much ownership and the potential profits that go with it. But early-stage angel funding may be the most useful money an entrepreneur gets, Alliance members emphasized. The right angel will find and correct a business's flaws, help make the firm more attractive to future investors, make key business contacts and defend the firm in future rounds of funding.

The 170-member Alliance of Angels is a group of individual investors and representatives of investment corporations, serving as a matchmaker for young technology companies and interested investors. For more information, see http://www.allianceofangels.com or contact Yvonne Muench, yvonnem@technology-alliance.com.