Angel Investing 201: The Basics of Impact investing

Agenda

• Stages of investing
• Why a Portfolio?
• Due diligence → better performing portfolio
• We invest in:
  – Companies whose mission is to help reduce social disparities, including addressing inequalities in health, educational and economic achievement, and treatment by the criminal justice system.
  – Companies whose mission is to help mitigate environmental damage and promote clean energy

• We recognize that each person in our diverse society has unique and valuable skills and insights.

• Some stats:
  – First investments in 2016
  – 83 angel investors
  – To date, have invested $8M in 27 companies
Stages of Investing

- Bootstrap
- Friends and Family
- Angels
- Venture Capital
- Strategic Investors
- Crowd Funding
- Kickstarter
- Grants
- M&A
- IPO
- Private Equity

Amounts raised:
- $0
- $x0,000
- $x00,000
- $xx,000,000
- $xx0,000,000

Exits

Time

Not all companies use all these stages.
Impact investing provides good returns

Impact Fund’s IRR compared with 75th percentile benchmarks as of 9/30/18

Kapor Capital Impact Funds Disrupts The Conventional Thinking on VC Investing

- KCAP: 29.02%
- Pitchbook 75th percentile: 25.96%
- Cambridge 75th percentile: 26.50%
What (ideally) happens when investing?

Assume you make equal sized investments in 10 companies.

Then, maybe five companies will provide a return, and one of those will give you a big win.
How Big a Portfolio?

- Minimum of 10
- 20 is better
Typical Time to an Exit or Going Out of Business

- Exits - 4 years 9 months
- Out of Business - 3 years 5 months

<table>
<thead>
<tr>
<th>Time</th>
<th>Exits OOB 0-24 Months</th>
<th>Exits OOB 25-36 Months</th>
<th>Exits OOB 37-48 Months</th>
<th>Exits OOB 49-60 Months</th>
<th>Exits OOB &gt;60 Months</th>
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<tbody>
<tr>
<td></td>
<td>17% (5)</td>
<td>17% (5)</td>
<td>3% (1)</td>
<td>17% (5)</td>
<td>14% (8)</td>
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<tr>
<td># of Companies</td>
<td>22% (12)</td>
<td>38% (21)</td>
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Positive returns occur at all investment amounts
Decide how much to invest in total

What percent of your assets do you want to put into this asset class, and over what period of time?

<table>
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<tr>
<th>$ per investment</th>
<th>Number of Investments</th>
<th>Total investment required</th>
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<tr>
<td>$5,000</td>
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<td>$250,000</td>
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<tr>
<td></td>
<td>20</td>
<td>$500,000</td>
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Reserve funds for follow-on rounds.
Improve Return Probability – Do Due Diligence
The Due Diligence Payoff

- < 1x return
- 1 to 5 x return
- > 5X return

- < 10 hours
- > 10 hours
Approaches to Due Diligence

• Go solo
  – Prepare to spend a week

• Be part of a team
  – Our angels working together

• Build upon diligence reports of others
  – Maybe this is a syndication deal and another team has put in many hours
Performing due diligence.

What to understand, and how to do it.
Due Diligence Goals

1. Gain confidence in the management team.  
   *The most important consideration!*

2. Gain confidence that the company will have significant social or environmental impact

3. Gain confidence that the company will become profitable and provide a return to investors
Team Validation – Job #1

What to understand

• CEO’s emotional maturity
  – Transparent, open, trustworthy, humble, coachable, always learning
  – Good team collaboration and communication skills

• CEO’s startup experience
  – Prior mistakes are good

• CEO’s domain knowledge of the company’s market

• Is this the CEO’s only gig?

• Appropriate titles?

• How does the C-level team work together?

How

• Phone calls
  – To direct references supplied
  – Ideally to secondary references shared by direct references
  – To former co-workers, board members, investors (LinkedIn is your friend)
The most basic Impact Test

• Does the company’s primary business mission clearly speak of impact?
  – Is impact part of their basic DNA?
• Is the CEO personally passionate about the impact mission?
• Does the company’s home page communicate their impact mission?
2nd major test - Efficacy

• What evidence is there that the company will effectively deliver significant impact?
• A must-have-impact for impactees?
• Effective plan for acquiring impactees?
• Long-term competitive impact advantages?
  – Higher adoption rates?
  – More significant impact?
• Direct impact?
Market Validation

What to understand

- Must-have versus nice-to-have
- Ability and willingness to pay for the solution
  - Revenue
  - Budgeted funds exist
  - If medical: FDA approval & insurance codes
  - Unpaid pilots don’t establish willingness to pay
- Are there enough of those payers to generate enough revenue (big market)?

How

- Phone calls with three to five payers
  - Understand their pain point and budget
  - Understand the sales channels they routinely use
- Try the product out
Go-to-Market validation

• Do they have a credible sales operating plan for scaling to enough revenue to allow acquisition?
  – What type of marketing and sales organization and partners do they need (internal and external)?
  – Not a plan: the CEO is today talking to the CEO’s friends

• How do they connect with potential customers?

• What is the cost of acquiring one incremental customer?
  – and retention rate
  – and lifetime revenue
Product/Technology Validation

• How ready is the product for full release?
• If SAAS:
  – Is the technology scalable?
  – Are developers tightly coupled to market validation?
• If hardware: is the supply chain in place?
• If medical: animal trials complete? Human safety trials complete?
Competitive Advantage Validation

• How significant is their competitive advantage?
  – Focus on customer benefit comparison and not feature comparisons
• Long-term, sustainable advantage => What keeps them successful for the seven years until acquisition?
  – Critical mass of customers?
  – Sales channel lock?
  – Supply chain lock?
  – IP/Copyright/trade secret?
Financial Validation

• Reasonable bottom-up details driving the financial model?
• Industry-normal investments in R&D and Marketing/Sales in out years?
• Revenue model
  – Bottom-up revenue plan based upon serviceable market
    • Number of customers willing to pay how much to solve a must-have solution
    • Not “we will get 2% of some huge market
  – Very small ramp => life-style business
  – Incredibly large => team not credible
Corporate Governance

• Who controls the company?
  – Capitalization table review
  – Does the CEO have the more ownership than other employees?

• Post-funding board structure?
  – Do investors have a seat?
  – Experience-level of board members

• Is legal representation experienced in startup corporate law?
Investor Return Validation

- With this investment, can the company achieve a business result that significantly increases valuation?
- Acquisition examples?
- What percent ownership will we achieve?
- Expected ownership percentage at exit and size of potential exit
  - Capital efficiency - what future rounds of investments are anticipated?
Investment Deal Terms

More Company Friendly

- Stronger company?
- Higher valuation cap or pre-money
- Higher risk of future down round?
- SAFE note

More Investor Friendly

- Easier to syndicate?
- Convertible note or preferred stock
- If we lead, we can set terms
- Lower valuation cap or pre-money
Portland Seed Fund is an early-stage venture fund in Portland and has made 70 investments.

They analyzed what parameters best predicted a high investment ROI.

By far, the best predictor of high ROI was company-friendly terms.

- Companies with the best products, the best teams and large markets can demand the best deal terms.
findings

Portfolio returns by key deal characteristics

Measured based upon valuation increase.
Leading round = negotiated the terms.
Capital Efficient = needs less than $5M total.
Additional Webinars

Angel Investing 101
- The Angel Experience: What is an Angel Investor? What motivates Angels? What are examples of typical Angel investments? How does the SWAN operate?

Angel Investing 202
- The Mechanics of Investments: Investment instruments, company valuations, dilution across rounds, post-investment activities, and tax considerations

Angel Investing 203
- Measuring Impact and Results: A Discussion of Metrics and Tools, and examples of SWAN impact assessments
Good Resources

![Angel Investing](image1)

*David S. Rose*

*CEO of Gust and Founder of New York Angels*

![Fundamentals of Angel Investing](image2)

*Hambleton Lord & Christopher Mirabile*
Webinar Feedback

Any final questions?  What was most helpful?  What was less interesting?  What would you like to learn more about?

To receive your webinar refund, please send your mailing address to bob.bridge@swanimpact.org