VENTURE CAPITAL

Angel investors spread their wings

By Beth Healy, Globe Staff, 11/25/2002

Angel groups used to be informal clubs, secret societies of elite techies with time and money on their hands. But the clubs are changing. They're opening offices, putting up Web sites, running small venture funds and, amazingly enough, holding national meetings to compare notes and set standards for what's become a booming little industry.

Angel investing can come in many forms, like an uncle writing a $500 check to help with a business venture. But it's most commonly thought of today as a collection of successful entrepreneurs who get together to review business plans and make small investments in start-ups related to their field of expertise. The outlays typically come at earlier stages and in smaller sums than investments from venture capital firms.

It became cool to belong to an angel group in the late 1990s, and the pastime drew all kinds of attention. Full books have been penned on the subject, along with studies by research groups. Meanwhile, the stock market has plunged, the tech sector is slogging through Siberia, and the economy stinks. Yet the most grounded of the angels are still out there, more eager to invest than ever, it seems.

"The angels have grown up," says James Geshwiler, managing director of CommonAngels in Lexington. Sure, the people looking for quick killings have disappeared from the scene, he says, but the number of formal groups has grown dramatically. "They're now taking a very disciplined approach," he says.

Jeffrey E. Sohl, director of the Center for Venture Research at the University of New Hampshire, last month published a study on the growth of angel investing in North America. By his count, there are 170 investment groups or angel networks in the United States and Canada - more than triple the 50 that existed five years ago.

The growth has been driven, Sohl said, by the number of people who made fortunes in the 1990s, and by the benefits these investors reap from the angel gatherings - social, intellectual, and potentially financial. In addition, Sohl found, there's a growing flow of deals making its way to angel groups, because they're willing to invest sums of $100,000 to $1 million, while VCs with giant funds typically want to put $3 million to $5 million on the line in early-stage deals.

While new angel groups are springing up, some that have been around for a few years are starting to develop brand awareness. Boston has CommonAngels, Walnut Venture Associates, Hub Angels, and Angel Healthcare Investors, just for starters. Virginia has its

Dinner Club, and Silicon Valley its Band of Angels, the biggest group in the nation.

"Each of us has a slightly different personality," says Geshwiler, who hosted the heads of all the Boston angel groups at his office two weeks ago. Last month, he attended a similar meeting of Silicon Valley angel-group managers. Those meetings followed an angel summit that was held at MIT last spring. Next, Geshwiler says, the angel community is planning a national event in Chicago to hammer out best-practices standards for the industry in terms of membership, investing approach, liability, and other issues.

It's angel investing gone corporate - or at least with a jacket and tie. Perhaps some angels learned how much there is to lose in a difficult market, as the entire VC industry has since 2000. Moreover, the sheer time involved in making savvy investments has jumped; angels - who often are repeat entrepreneurs and ex-CEOs - need more behind-the-scenes help now in sorting through business plans, responding to telephone calls, and coordinating with members to make investment decisions.

Robyn Davis and Mary McNamara are co-managing directors of Angel Healthcare Investors, a Newton group of 45 life-sciences, biotech, and services entrepreneurs. They have just recently launched the group's Web site (www.hcangels.com) and have overseen $7 million in investments in 16 companies in three years. The group typically coinvests with venture firms; total funds raised by companies backed by Angel Healthcare over the period is $500 million.

Davis says the group reviews 25 to 30 deals a month; they're usually referred by people in the group or their acquaintances. It's rare for potential deals to come in cold. Of those, two are selected for formal presentations to the angels at monthly meetings. "What the entrepreneurs get is feedback, basically free consulting, from 40 people," Davis says. "Even if they don't fund you, that's very valuable."

It's the culture of these angel clubs that is so intriguing, and appears to have made them into lasting organizations. They're usually created by well-known people in a particular industry, who then attract other executives and entrepreneurs highly respected in the same field.

Angel Healthcare, for instance, was launched by Alan Solomont, a health care investor who founded ADS Group, a provider of elder care services in New England. The late Susan Bailis also was a founding member; she was associate director of the New England Medical Center and a professor of psychiatry at Tufts University School of Medicine. Their third partner: Richard N. Thielen, CEO of Rinet Co., an investment firm he merged into Boston Private Financial Holdings in 1999.

"People did very well in the '90s, but they didn't want to retire and play golf," Davis says. "These are groups of people who come together around an industry or interest and want to put their money to work together, and want to take a more active role in working with companies."

CommonAngels is all about software. The group was started by five members of the Massachusetts Software & Internet Council in 1998, and it's grown to 55 members. The roster includes John Landry, the former technology chief at Lotus Development Corp. and vice president of tech strategy at IBM; he's now CEO of Adesso Networks. Charles Stuckey, chairman of RSA Security, joined in the spring. John Cullinane, founder of Cullinet

Software, also joined this year.

CommonAngels, which holds its monthly meetings over breakfast at the Four Seasons, has invested $32 million in software deals. That's the sum of individuals writing checks of $100,000 or so to entrepreneurs who've presented their business plans. In addition, the group has a $10 million fund, made up of members' pooled funds, which invests in deals. In a shock to everyone, the group recently backed a chip deal, Sand Video of Andover, the first time CommonAngels has veered from software.

"I kept telling them, `We'll listen, but we're not going to fund you. We're software,' " Geshwiler says. At the first presentation, several CommonAngels members tried to persuade Sand Video's founders to come up with software technology for their video-compression project. Founders Don Shulsinger and Peter Besen went back, thought about it, and returned with a more thorough explanation of why they needed to make chips to improve the handling and manipulation of digital images. At the end of the meeting, Geshwiler says, the angels wanted to invest. "We had $1 million in 10 minutes."

Some observers wonder what's next for these increasingly organized and sophisticated angels. Might they morph into full-fledged venture firms one day? For the moment, angels say they simply want to complement traditional VCs, by filling an early-stage funding gap and lending the know-how of experienced entrepreneurs. In addition, many angels don't want the responsibility for outside money and a huge portfolio. As Geshwiler sees it, "This is becoming a tier, an institutionalized tier of venture funding."

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