BUSINESS ANGEL INVESTING

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Everything you need to know about investing in unquoted companies

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ABOUT THE AUTHOR

Richard Hargreaves read engineering at Cambridge and then studied for a PhD in Electrical Materials Science at Imperial College. After a short spell at the then Science Research Council, he joined ICFC (now 3i plc), which was the principal source of long-term capital for UK private companies until the late 1980s. After ten years of making investments in unquoted companies, he left to start Baronsmead plc, which he developed over 13 years until its sale in 1995. During this period, Richard was actively involved in the growth of the venture capital industry through the British Private Equity & Venture Capital Association (***BVCA***[1]), where he became chairman. At BVCA he was involved with their tax incentive lobbying, which saw the birth of the VCT, and Baronsmead's name is still on several of the best performing VCTs.

After its sale, he managed Baronsmead for two years before he started Classic Fund Management Ltd. He sold that company in 2004 and co-founded Endeavour Ventures Ltd, which invests in young technology companies for its client base of high-net-worth individuals. He retired from Endeavour in 2018 to focus on being a professional business angel investing only in ***B2B*** software-driven opportunities.

Richard has nearly 50 years' experience investing in young companies and helping them to grow. He is an experienced non-executive director and professional business angel with significant understanding of the US market.

1 This format is used for words/phrases which are more fully described in the Glossary.

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There are many people who have helped me with this book, though not all are aware of it.

My particular thanks go to Tyler Crown who went through every word with me and researched the sources of much of the quoted data. I also need to thank Magnus Macintyre who copy-edited the text before it went to the publisher.

My ex-colleagues at Endeavour Ventures all played a role too as they were involved with most of the examples used in the case studies and went through many of the highs and lows with me.

Finally, I need to acknowledge those who ran, or run, companies in which I invested and who indirectly contributed to this book. Many of the case studies use experiences from those investments though most of the companies are not named.

Thank you all for the rich experience I have enjoyed.

PREFACE

THE FIRST EDITION of this book was published in 2013 under the title *How to Become a Business Angel: Practical Advice for Aspiring Investors in Unquoted Companies.* Private individuals were then the UK's most important source of equity capital for companies seeking less than £2m, and it remains so. However, much has since changed in the world of financing unquoted companies, which is the reason for a very revised second edition.

The book covers all aspects of investing in unquoted companies as a private individual. It offers practical guidance to those who wish to make such investments for the first time and to those who have invested before but who would like to develop a more systematic approach. The content is also relevant to those investors who do not see themselves as business angels but do invest in EIS opportunities through their financial advisers and would like to learn more about the risks and rewards of unquoted investments.

The book discusses how to find investments, assess them, structure them, manage them and finally – and importantly – exit from them.

I have invested in private companies for most of my life and I have had many successes and many failures. So I do know a lot about the ups and downs of backing smaller companies and would not swap the excitement and satisfaction of that for something less challenging. If my experiences and thoughts encourage some to become involved – or more deeply involved – with this fascinating activity and, at the same time, help improve their chances of success, it will have served its purpose.

Richard Hargreaves,
April 2021

FOREWORD BY LORD FLIGHT

This is a great book, which I commend strongly to the Treasury. The professional research entailed is most impressive and useful. I write as Chairman of the EIS Association: Richard is setting out how much of our economic growth and job creation has come from entrepreneurial businesses over the last decade – a fundamental point of which I have sought to get across to the Treasury.

Richard has had a remarkable and impressive career. I am interested to note he has a Cambridge degree in engineering – over my 50-year career in the Investment Management industry, and more latterly Small Cap, I have invariably found the ablest people have impressive engineering degrees. Richard's career has also been top quality, starting at what is now 3i plc; moving on to start quality Small Cap investor Baronsmead; then Chairman of the BVCA and co-founder of Endeavour Ventures Limited which invests in young technology companies.

Richard has been one of the key British Angel Investors. A combination of Venture Capital and EIS investing has created the major development of venture capital investing in Britain.

Richard's book includes a useful list of the key characteristics of angel investors' and VCs' differences. Richard also analyses the profile of a typical UK Business

Angel investor and lists what he sees as the 10 key requirements for being a successful angel investor.

I would recommend strongly that a copy of this book is given to all school sixth forms and university libraries.

Lord Flight,
Chairman of the EIS Association,
December 2020

FOREWORD BY TIM MILLS

The world of angel investing can at times appear shrouded in mystery, a clubby place where covens of self-styled dragons determine the fate of courageous would-be entrepreneurs from the comfort of their high-backed armchairs. Dismissing the hopes and ambitions of those before them on a whim, with a curled lip and a raised eyebrow for good measure. The metaphoric thumbs up or 'I'm in' guaranteeing the success of the hopeful, in return for a hefty slice of equity and a piece of the soul, and thumbs down ('I'm out') condemning them to near certain failure.

Although I think most people recognise the theatre for what it is, and that is simply theatre, the image sticks and it's not a helpful one for either investors or entrepreneurs.

Adding to the challenge for anyone with an interest in investing in unquoted companies is that when you get beyond the pretence and spin, most of what does get written on the subject every year is often nothing more than the relaying of received wisdom. There is little out there that falls into the category of being particularly actionable or useful, and almost nothing of reference should you wish to consider the performance of your own investments.

Going some way to filling this void, Richard gives us here one of the very few open and quantitative accounts of the reality of investing in early-stage businesses. Blending together a practical guide, where possible informed by what data there

is in the public domain, but critically placed alongside illustrative examples and anecdotes from personal experience. Offering detailed insight on both the highs and returns to be made, when things go well as well as the lows and challenges that arise, and what can be done to mitigate them.

The frankness of his appraisal of what worked and what didn't and what lessons really can be considered transferable is refreshing in its openness and pithy with its honesty. No attempt is made to disguise the risks with this type of investment, of which there are many, but equally the upside of success is plainly stated. He doesn't scrimp in highlighting the need for professionalism and rigour on the part of the investor, as even though the risks may be significant, blind punting rarely achieves the desired outcomes.

I have had the privilege of joining Richard in a number of investments over the past decade and some have gone tremendously well and others not so, but all have begun with belief in the potential of a team and the opportunity to build and scale a business. The path that follows from the day the shares get issued is rarely straight and almost certainly never quite the one you expected, but the journey is rarely dull.

There is however certain knowledge that can save some easy, and expensive, missteps and in this book Richard highlights but also manages to clearly explain why the golden rules of successful venture investment hold true. Showing that an investor must be active (or at least ready to be so) to support companies and deal with issues that arise; that upfront due diligence is key, but can only ever reveal so much; that an investor always needs to be able to follow their investment (and hence needs to retain some reserves); and that even the best don't get it right every time, so building a portfolio is key.

Although there are few investors around who can claim Richard's depth and range of experience in backing high-growth companies, the following pages share insights that would benefit even the smallest scale angel and certainly those with ambitions to build larger portfolios. But as Richard clearly shows, the returns when you get it right make what can often be a series of roller coaster journeys fully worthwhile.

Tim Mills,
Managing Partner ACF Investors who manage The Angel CoFund,
January 2021

INTRODUCTION

To be a business angel is one of the most exciting investment opportunities available to you as the scope for profit is unlimited. Bob Dylan illustrated the excitement when he wrote *The Stranger Song*, which includes the line:

> "Like any dealer, he was watching for the card that is so high and wild he'll never need to deal another."

That is the holy grail where that one elusive investment pays for all the others and makes you a very handsome overall return.

Many people find the idea of helping entrepreneurs enticing and are attracted to the financial rewards it can offer. Helping finance young businesses not only offers the potential of large profit but also the opportunity to help companies grow and the chance to see success built from nothing. There is, too, the added satisfaction of helping the UK's economy without spending money – the more successful a business becomes, the greater its contribution to economic growth and the greater your profit.

In recent years, there has been a new industrial revolution resulting from a tsunami of advances in computers, reductions in the cost of data collection and storage, and the near saturation of smartphone ownership. These advances have created myriad opportunities for startups to disrupt the status quo and have led to a massive increase in funding opportunities for private investors as almost all startups are financed by them.

The UK needs angel investors. Much of our economic growth and job creation

comes from innovation and most of that takes place in early-stage entrepreneurial businesses. Such ventures have never been well served by banks or professional venture capital, and the importance of angel financing has been recognised by government for many years. One result of this is there are attractive tax incentives available to private investors.

However, there are high risks involved and serious angel investing is about balancing risks and rewards to make money over what can be long periods of time for any one investment. Patience and the ability to remain calm in the face of adversity are essential.[2]

This book argues for a systematic approach and it cannot be stressed too strongly how misleading the razzmatazz of the TV series *Dragons' Den* is in presenting this world. The TV dragons are portrayed as expert investors but the reality is different. Research has shown that better investment results would have come from backing a random sample of startups rather than the investments the dragons have made over the years.[3]

The book draws on my own experiences as a venture capitalist as well as my own wide experience as an active angel and non-executive director. As you will see in Chapter 2, there is little published data on the investment returns angels make, so I have used my own data as a detailed example of what a mature portfolio might look like.

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2 The information contained in this book does not constitute legal or financial advice. There are many references to legal and tax matters, all of which should be verified before making investment decisions. You should never make any investment decision without first conducting your own research and due diligence.

3 www.growthbusiness.co.uk/random-investment-startups-dragons-den-2556106

PART A
ANGEL INVESTING

You will find it helpful to have some understanding of the role angel investing plays in the financing of early-stage growth companies. It has different characteristics from other long-term investments and you need to understand the differences.

It is easy to appreciate the obvious appeals of angel investing, but you also need to be fully aware of the concomitant risks before committing to this high-risk activity.

CHAPTER 1
How do business angels fit into the overall spectrum of long-term capital?

The importance of angels

Angels

The term angel was first used to describe wealthy individuals who financed Broadway productions. Then in 1978, William Wetzel published a study on how entrepreneurs raised seed capital in the US and used the term to describe the investors.[4]

Today, ***business angel*** (or just ***angel***) is widely used to mean a private individual who invests their own money in early-stage companies.[5] The other principal source of long-term investment in such companies is ***venture capital (VC).***

4 www.rcbi.org/index.php/viewarticle/49-capacity-magazine/spring-2014/features/667-angel-investingit-s-an-increasingly-important-part-of-today-s-business-landscape

5 Terms in bold italics throughout the book are defined in the Glossary.

The scale and importance of angel financing

Whilst there are published studies on angels, there is a paucity of research on the returns that can be made from angel investing. This is at odds with the importance of them as a source of finance.

US

The US, as a pre-eminent innovatory culture, was the founder of both modern venture capital (VC) and angel investment, so its data is worth reviewing. Whilst it's hard to pinpoint an exact number, the Angel Capital Association estimates there are approximately 300,000 angel investors in the US.[6] In 1996, the number of angel groups (or investment syndicates) was ten and it rose strongly to over 200 by 2006. VCs do not typically invest below $1–2m and angels are needed to fill that ***equity gap***.

Angel financing is very important to the US economy. In 2012, it provided $23bn to 67,000 companies creating 274,800 new jobs, compared to $29bn of VC funding into 3,752 companies.[7] The average amount of money raised from angels was approximately $340,000 compared to nearly $8m from VCs, which emphasises the importance of angels at the smaller end of the market. Technology was the predominant venture-backed startup industry and Silicon Valley businesses accounted for 40% of all angel investments. Almost all major US technology companies were funded in the early stages by angels. These include Microsoft, Apple, Google, PayPal, Facebook, LinkedIn and Netflix.

The technology boom that exploded in the last few years led to VC investment mushrooming to $130bn in 10,777 deals in 2019.[8] Angel investment no doubt also mushroomed but figures are not yet available.

UK

As in the US, angels make a significant contribution to the UK economy. Oxford Economics assessed the economic impact on the UK of firms using VC or business angel finance. They identified 15,000 angel-backed businesses over

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6 www.angelcapitalassociation.org/faqs

7 rtp-equity-static-origin.s3.amazonaws.com/email/investopedia201309/RockThePost_Report_What_Angel_Investors_Know_About_Startup_Investing_Sept2013.pdf

8 nvca.org/pressreleases/us-venture-capital-investment-surpasses-130-billion-in-2019-for-second-consecutive-year

the five years to 2015 and estimated they had a combined turnover of £9bn, contributed £4.5bn to GDP and created 69,700 full-time equivalent jobs.[9]

There have been several studies of angel investing in the last few years of which the best, in my view, is the 2018 British Business Bank study *The UK Business Angel Market,* which is based on a survey of 650 angels made in conjunction with the UK Business Angels Association.[10] The study's central message is that angels "*play a vital role in the economy, bringing patient capital, business experience and skills to support growth of smaller businesses*" and its main conclusions are:

1. The UK business angel market is maturing. More than 50% of angels have more than five years' experience as an investor. The angels surveyed made more than 2,500 equity investments in 2016/17 and four out of five invested as part of a syndicate.
2. Angels invest patient capital. The average duration of an investment is six years.
3. Angels can help entrepreneurs with business and fundraising.
4. 57% of the angels and the businesses they supported are in London and the South East.

There is no doubt that government tax-advantaged schemes have been a major factor in this growth.

Where angels fit within the financing spectrum

Investment by angels is a vital bridge between startup finance from friends and family, on the one hand, and growth finance from VC, on the other.

Friends and family

Almost all aspiring entrepreneurs need money from others. The first port of call is usually friends and family. They are loyal and helpful investors, but many

9 developmentbank.wales/news-and-events/what-angel-investing-and-why-become-angel-investor

10 www.british-business-bank.co.uk/wp-content/uploads/2018/06/Business-Angel-Reportweb.pdf

business ideas cannot be developed fully without more cash than they can provide.

Banks

A bank might remortgage an entrepreneur's house to provide money, but otherwise they are not helpful with early-stage ventures. They want to see readily realisable security for the money they lend and firm evidence that it can be returned from the cash flow of a business. Most startups simply cannot provide this. If a loan is offered, the bank will usually ask for personal guarantees, so the entrepreneur's risks can increase to the possible loss of the family home.

Venture capital

The entrepreneur often thinks of VC firms before angels if only because they are easy to find and VC backing is seen by some as a status symbol. The availability of VC in the UK increased dramatically during the second half of the 20th century.

In the 1970s, the principal source of such capital was the Industrial and Commercial Finance Corporation (ICFC, since renamed 3i), which was founded in 1945 with government encouragement and the backing of the clearing banks.[11] ICFC dominated the market until the mid-1980s when independent VC firms began to flourish.

In the early days of independent VCs, they backed many startups and small ventures. Over time, however, most of the industry migrated upmarket to become today's ***private equity (PE)*** groups because of the easier and less risky returns. As a result, VC for early-stage companies became harder to find.

In contrast to VC, PE groups typically buy – not back – existing companies with predictable cash flows, investing equity alongside huge sums borrowed from banks. They then incentivise management with significant equity stakes.

Such transactions are compelling for PE firms. The large size of the deals means the management fees (1% to 2% of capital managed) pay the PE team fat salaries. Added to this are performance fees (typically 20% of profits made after the benefits of heavy leverage from bank debt).

All of this means the PE partners get rich provided they hire the right

11 www.civitas.org.uk/pdf/ICFC.pdf

management to run their companies and the economy is stable so that leverage works for, and not against, them. The financial collapse in 2008 did, however, bring the risks of the highly leveraged deal into sharp focus, as did the Covid-19 pandemic in 2020.

When the first edition of this book was published in 2013, there was only a small number of specialised VC firms that still invested in startup and early-stage ventures. An increase in government-sponsored regional funds helped with the supply of funding, but it still left an equity gap to be filled by angels.

At the end of the 20th century, we saw a dramatic explosion of entrepreneurial activity seeking to exploit the opportunities presented by the internet (the ***dotcom boom***). Much of this ended in tears (Amazon being a very notable exception) as the technology was not then capable of delivering on its promise. However, in more recent years, there has been a second dramatic growth in entrepreneurial activity driven by extremely rapid advances in technology. Fundamental to this was the explosive growth of the internet, cheap sensors, WiFi communication and, crucially, the smartphone becoming ubiquitous. Many of the tech company startups founded to exploit these opportunities grew fast and made investors lots of money. This, in turn, led to a rapid growth in VC funds keen to back early-stage tech companies and companies that use the internet to sell or promote their products or services.

The most recent VC funding figures are extraordinary. UK early-stage companies raised more than £10bn in 2019, an increase of 44% over 2018.[12] Interestingly, US and Asian funds accounted for approximately half of this investment. The amount invested in the UK was a third of total European investment.

One interesting phenomenon is the rise of giant global funds, the largest of which is SoftBank's $100bn Vision Fund run by Masayoshi Son. He invested $20m in Alibaba, which became worth $60bn at ***Initial Public Offering (IPO)*** and double that later.[13] However, he then got carried away and invested huge sums at high valuations in many ventures, including the disastrous WeWork. His exuberance was at the centre of a VC feeding frenzy – companies were encouraged to ignore financial fundamentals in pursuing winner-takes-all deals with extravagant valuations and expectations driven by fear of missing out on

12 www.telegraph.co.uk/technology/2020/01/15/uk-tech-investment-surges-record-101bn-2019-despite-brexit-fears

13 www.reuters.com/article/us-softbank-group-alibaba/softbanks-son-sticks-with-gut-led-investing-in-chat-with-alibabas-ma-idUSKBN1YA0HB

the next big winner. Sanity will no doubt return, but the over-exuberance has affected angel investment by raising unrealistic expectations of the valuation many entrepreneurs believe they can put on their ventures when raising money.

The huge recent growth in VC investment does not mean that the angel has been displaced. Far from it, as the angel remains crucial to the early development of new ventures in the continuing role of funding the equity gap between friends and family, and VCs. Alongside this, the tech revolution has resulted in many more ventures seeking money.

Government stimulus for angel investing

The UK government has long recognised the importance of angel funding to the creation and growth of new companies, which, in turn, are important to economic growth. There are two main tax-advantaged schemes available to the angel. These are the ***Enterprise Investment Scheme (EIS)*** and, a more recent scheme, aimed at very small startups and closely modelled on the EIS, called the ***Seed Enterprise Investment Scheme (SEIS)***.[14]

To help angel syndicates raise the total needed for a venture (which can be challenging), the government launched the Angel CoFund in 2011. It is now a £100m fund that is prepared to invest alongside a syndicate of angels and on similar terms.[15]

Why angels are attractive investors

How angels and VCs differ

As funders, business angels have three key attributes:

1. They provide up to £1–2m or more in funding (usually as a syndicate).
2. They provide 'smart capital', offering business experience and introductions to help early-stage businesses grow.
3. They provide 'patient capital', which recognises it takes time to develop a successful business.

14 Both are described in detail in Chapter 7.

15 See 'The Angel CoFund' on page 71.

They also have a number of other characteristics that are quite different from other investor groups – particularly VCs:

1. **Angels invest their own money whereas VCs invest other peoples' money structured as a fund.**

   This makes the angel a sympathetic and supportive investor. They can be more loyal and less brutal when hard decisions have to be made. They will also work harder to protect their own money – a normal human trait. VCs have timescales determined by their fund structure, which can lead to pressure to exit by a certain date. The angel has no such restriction.

2. **Angels are quick decision makers. They don't need to consult others when they invest – in contrast to VCs.**

   Many angels make decisions based on an informed view of the opportunity and a liking for the management team. ***Due diligence*** is usually a softer process than with venture capital.

3. **Angel syndicates can be difficult to pull together because they make decisions independently of each other, whereas a VC writes one cheque.**

   A major issue with angels is pulling the syndicate together. It can be very helpful to have a facilitator, which is what angel networks and syndicate managers do.

   Despite this, the VC's ability to write one cheque does not mean a VC is faster to invest.

4. **Angels will usually opt for a simple investment structure and ask for simpler controls on decision making as the venture develops.**

   Typically, a VC will demand priority over other investors for the return of their investment and will demand close control of corporate decision making.

5. **Angels can add value from their own experiences and contacts.**

   Many angels are older and more experienced than most executives in VC firms. They can offer valuable advice, mentoring and contacts to the entrepreneurs.

6. **Angels are less punitive in their approach to further investment when things don't go to plan.**

7. **VCs can be ruthless if projections are not met and further funding is required. That is, of course, not a good moment for a company to**

approach its investors with cap in hand. Angels, on the other hand, tend to be more understanding in those circumstances and the terms they then demand are often softer.

Most of these characteristics make angels a very attractive source of capital.

The combination of quick decisions and the ability to bring directly relevant experience and contacts to the table is particularly appealing to entrepreneurs. So is the relative simplicity of the investment documentation.

Angels are also good at following on with further money when the business needs it, and if one or more members of the syndicate drops out, that does not mean the financing round fails.

CASE STUDY 1.1 ANGELS CAN FIGHT BACK

I joined the board of a US technology company as an independent director six months before the company planned an AIM market flotation. Top of the agenda at the first board meeting was bridge funding. This was to be a convertible loan with 10% rolled up interest that would convert into shares at half the IPO price. As these terms seemed somewhat egregious to me, I spoke to the CEO before the meeting to understand what was happening.

The company was nine years old and had been mainly financed by Silicon Valley VCs. However, the company had its ups and downs but was growing fast by this time. It had raised a total of $90m and now needed $15m more to reach the proposed IPO.

The VCs proposed very harsh terms that would have resulted in non-participants' shares becoming worthless. This annoyed the angel investors so much that a syndicate of them underwrote a convertible loan to replace the VC offer. The underwrite meant that the VC offer was dead and, ironically, several of them invested in the loan. In the event, the IPO took 16 months, but as shares opened at a 40% premium to the IPO price, the convertible loan note holders made just over three times their money.

POINT TO NOTE: VCs do not always get their own way.

Summary

Angels are extremely important to the development of innovative young companies. They are a vital presence amongst the providers of long-term capital and essential when ventures need £2m or less of equity capital.

The angel is also often the most welcome of all investors because of the speed of decision making, simplicity of investment structure, the ability to add value and a willingness to be patient.

CHAPTER 2
What do angels look like and do they make money?

THIS CHAPTER LOOKS at the profile of the typical UK angel about which there have been several studies.

Unfortunately, there is a paucity of published research on the investment returns made by angels. The reason is that researchers do not have access to detailed comparable angel investment performance data even when they invest through angel groups or syndicates. To demonstrate that angel investing can be worthwhile financially, I have used my own portfolio as a detailed example.

Who makes angel investments?

The profile of a typical UK business angel who responded to the 2018 British Business Bank survey shows:[16]

1. They are male, white and live in the South East.
2. They have an average age of 52 – 21% are over 65.
3. They have eight years' investment experience with 56% having more than five years.

16 See second paragraph on page 7.

4. About 65% have made ten or fewer investments.
5. The most experienced angels invest 22% of their investible wealth while the less experienced invest 14%.
6. The median first investment is £25,000 with a median follow-on investment of £7,500.
7. Some 79% of angel investment is done as part of a syndicate which allows larger sums to be invested than any one angel would do.
8. They spend 1.6 days a week on angel activities.
9. They hold their investment for six years with the less-experienced angels expecting a shorter timescale than those with the most experience.
10. They make use of the EIS and SEIS schemes, with the majority investing in riskier businesses or in larger amounts if EIS or SEIS reliefs are available and many only investing if the schemes are available.

What companies do they invest in?

Angels invest across all commercial sectors, but in recent years angel investment has been dominated by technology. Major sectors in technology include financial services (fintech), healthcare, ecommerce, biotech and ***Software as a Service (SaaS)***.

Investment returns

Some 53% of angels thought their portfolio met expectations and 16% said their portfolio exceeded them. Interestingly, 58% of angels above 55 years of age thought their portfolio met expectations and 19% said it exceeded their expectations, whereas the numbers for those angels under 55 were 47% and 14% respectively.

The two principal reasons for expectations not being met were poor management and a need for more money than anticipated.

The survey also found:

1. Some 56% of investments made were either completely lost or failed to return the amount invested.

2. Some 30% of investments realised between one and five times the initial investment.
3. A total of 14% realised more than five times the initial investment.
4. For successful investments, the commonest exit route was a trade sale.
5. Angels often must hold most of their investments for more than ten years.

This pattern of performance is a fundamental characteristic of early-stage investing. It means you must seek high returns on each investment so the good ones pay for the failures and the portfolio produces an overall profit.

Strategies that improve investment outcomes

There was a 2009 survey of angel investing by ***National Endowment for Science, Technology and the Arts (NESTA)*** in conjunction with the UK Business Angels Association called *Siding with the angels*.[17] Although it pre-dates the British Business Bank survey and only collected data from 158 angels, it too is worth reading.

That study concluded there are four strategies that can materially improve the chances of success:

1. An angel should stay close to their entrepreneurial and industry expertise in choosing investments.
2. Even a relatively small amount of due diligence can help avoid failures.
3. Post-investment interaction is valuable but close involvement in a managerial role is to be viewed with caution.
4. Follow-on investments are significantly related to lower returns because of the tendency to try to save a failing investment.

Points 1 and 2 are related. If you know about an industry from experience, you will be aware of proven business models, market dynamics, obvious pitfalls and what innovations are likely.

Although the NESTA report is older, it has some data on investment returns that the British Business Bank survey does not. It found that the mean return from exited deals was 2.2× the amount invested. This figure should be viewed with caution as a final portfolio score would need all deals to have been exited. I have

17 www.effectuation.org/wp-content/uploads/2016/06/wiltbank-business-angel-investing-1.pdf

used my own data below to give a more complete picture, but it is, of course, simply one person's experience.

In contrast to angel investing, there is much more published data on VC returns. A 2019 report by the British Business Bank, *Analysis of UK VC Financial Returns*, is a good example.[18]

My investment experience and returns

In this illustration of the returns that can be made from angel investing, I have included all my investments made since 2004 when I became a serious angel investor.

In summary, from mid-2004 to mid-2020 I invested in 42 companies (32 of which were ***tech***) and the investments and returns are summarised in Tables 2.1 to 2.4. My portfolio return expressed as a multiple of money invested (taking account of all ***EIS reliefs*** on those investments that qualified) is 8.0× after tax for all investments and 10.1× for the tech investments alone.[19] You should note how much lower the returns would have been if EIS reliefs had not been available.

Overall summary

Table 2.1 My portfolio returns with and without EIS

	ALL INVESTMENTS	
	ALL	TECH
Number of companies in which investments were made	42	32
Returns if there had been no EIS reliefs		
Multiple of investment achieved	5.1×	5.7×
Returns after EIS reliefs		
After EIS upfront tax relief	5.8×	6.5×
Net of income tax relief on EIS losses	6.2×	7.2×
And with ***CGT*** deferral	8.0×	10.1×

18 www.british-business-bank.co.uk/finance-hub/wp-content/uploads/2019/10/BBB-VC-Financial-Report-FINAL-VERSION-17Oct2019.pdf

19 EIS reliefs are discussed in Chapter 7.

Notes

1. Returns with no EIS reliefs are stated before CGT.
2. EIS reliefs were only claimable on 71% of investments.
3. When EIS reliefs were claimed there was no CGT to pay.
4. 'CGT deferral' is referenced in Note 4 in Table 2.3.

Investments

Table 2.2 A breakdown of investments made

	ALL INVESTMENTS	
	ALL	TECH
Number of companies in which investments were made	42	32
Average number per year	2.6	2.0
Average first round investment amount	£61k	£66k
Average number of rounds per company	2.8	3.0
Average further round investment	£21k	£22k
Average first and further investments per year	7.3	6.0
Total number of investments made	119	97
Number of EIS qualifying companies	30	23
% of EIS investments	71%	72%

	EXITED INVESTMENTS	
	ALL	TECH
Number of companies	32	22
Average exits per year	2.0	1.4
Number of EIS investments	20	10
% of EIS investments	63%	43%
Average years from first investment to exit	5.3	4.9

Notes

1. I have made no investments as a sole investor. They have all been made as part of a syndicate and I have led 20 of the tech syndications but only one of the non-tech ones.

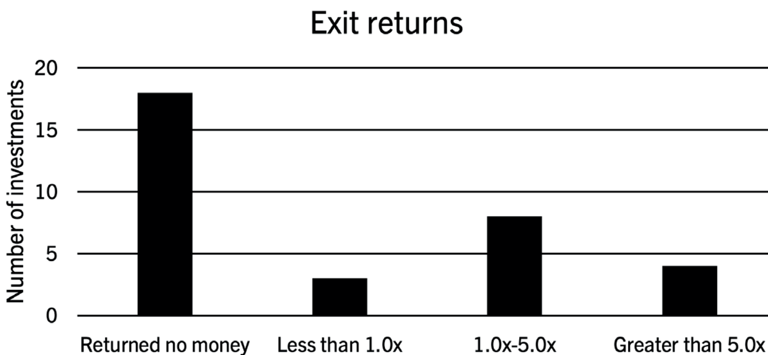
2. ***Tech*** companies are investments made in the technology sector. In the early days some were medical, but since 2008 all have been ***B2B*** computer technology using the software, data and internet advances of the last ten years. This is the sector I know most about and from which I have had the best returns.
3. The investments in each company have varied from one round to (I am embarrassed to say) 14.
4. Nine of the companies have had down rounds and four of these have effectively been ***wipe out*** rounds. I invested in all four and saw a successful exit in three, with one still held and increasingly likely to show a positive return.
5. Eleven of the companies (all technology) have had changes at ***C level (CEO, COO, CFO or CTO)***. One of them has had four CEOs and three CFOs.
6. Eleven of the companies have a US presence or significant sales made from the UK.
7. Nine out of 42 companies had VC investment (including government supported regional funds and corporate VCs) and five had investment from the Angel CoFund.
8. All but five of the companies were at an early stage of development.

Only seven of the 42 achieved positive ***EBITDA*** during the investment holding period.

Exits

I have had 32 exits, leaving me with a portfolio of ten companies. Of these exits 22 were tech companies. The average time from investment to exit was 5.3 years.

Figure 2.1 The overall return is driven by a few big winners



Investment returns

Table 2.3 Investment returns with and without EIS

	ALL INVESTMENTS		EXITED INVESTMENTS		ZERO SCORE ON INVESTMENTS STILL HELD	
	ALL	TECH	ALL	TECH	ALL	TECH
Returns if there had been no EIS reliefs						
Multiple of full investment	5.1×	5.7×	4.3×	5.0×	2.7×	3.1×
IRR	22%	30%	22%	31%	19%	28%
Returns after EIS reliefs						
After EIS upfront tax relief	5.8×	6.5×	4.5×	5.3×	3.1×	3.6×
Net of income tax relief on EIS losses	6.2×	7.2×	5.3×	6.1×	3.9×	4.7×
And with CGT deferral	8.0×	10.1×	6.1×	8.8×	4.2×	5.4×
IRR	31%	**42%**	31%	**43%**	29%	**40%**

Notes

1. *'All investments'* assumes that the remaining ten investments exit as per my current predictions whereas 'Zero score on investments still held' assumes these investments all fail, which confirms that my overall returns are not dependent on assumed high exit values from existing investments. Investments still held are valued on what is believed to be a realistic basis – often the last funding round price.
2. *'After EIS upfront tax relief'* takes account of the 20% upfront tax relief until 5 April 2011 and 30% thereafter.
3. *'Net of income tax relief on EIS losses'* assumes income tax relief at 45% is claimed on all losses (net of upfront tax relief on EIS losses).
4. *'CGT deferral'* is after allowing for ***Capital Gains Tax (CGT)*** rollover relief.[20]
5. Returns with no EIS reliefs are stated before CGT.
6. EIS reliefs were only claimable on 71% of investments (see Table 2.2).
7. When EIS reliefs were claimed there would be no CGT to pay.
8. IRR is the internal rate of return.[21]

20 See 'Capital gains tax rollover relief' on page 85.

21 See 'Internal rate of return' on page 72.

Involvement

I have been closely involved with 24 of the 42 investments and a non-executive director of 18 of them.

I am closely involved with six of the ten companies currently in my portfolio. All but one look likely to make attractive returns.

My experience

1. My personal profile is not dissimilar from that reported in the British Business Bank survey summarised earlier in the chapter, as are my exit experiences and the average time of investment holding. I have spent approximately three days a week building and managing the portfolio.
2. My returns are better than the 2.2× quoted in the 2009 NESTA report and my tech returns are much higher than my non-tech ones (which were poor and returned less than money invested before tax reliefs).[22] The IRRs are respectable too. And ironically, my portfolio of tech businesses suffered far less than most during the 2020 Covid-19 pandemic with three companies experiencing increased rates of growth.
3. I have made many bad mistakes – the company where shareholders made 14 investments before admitting failure being an example of putting good money after bad.
4. Down rounds are not always bad news for those brave enough to invest further. I have done well from them.
5. Many of my investments have US sales, presence or residence as most are software companies that commonly seek growth in that market.
6. Change of management is something with which a closely involved investor must help as change is not usually voluntary. Only twice have I seen a founder CEO offer to stand aside when he thought somebody else could do the job better.
7. A strong deal flow is vital to make angel investing successful, as is a well-planned approach.

22 See Table 2.1 on page 18.