

Business Financing With Venture Capital and Angel Investors

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The President of the Dallas Fed Bank said our economy is strong, in part, because of a “robust Entrepreneurial spirit.” That spirit is an essential element in any progressive economy, but to have a really world-class economy, strong equity financing organizations and mechanisms have to be available.

Equity financing is simply selling part of the business, or, giving up part ownership in return for the cash necessary to build the business. Equity financiers invest in a business in hopes of receiving a higher than average return on their investment.

Two major equity financing mechanisms are Venture Capitalists (VCs) and Angel Investors.

VCs became popular throughout the rise of the dot-com bubble of the '90s. VCs were also credited with fueling the bubble burst in the late '90s by pumping massive amounts of money into companies that ignored the most basic economic principle of business: No profit = No business.

VCs are not a funding option for the average Entrepreneur because most only look at super high growth potential firms... “gazelles.” VCs invest in high risk, high potential companies expecting an extremely high rate of return on the investment. VCs and their investors are very sophisticated and usually very actively involved in the businesses they invest in.

VCs act much like investment brokers, investing other people and institution's pooled money into companies that they work very closely with. Most VC's minimum investment is \$2-4 million or more. They expect to lose on 14 out of 15 investments, but on that one out of 15 they expect to make a high enough return to more than make up for all losses.

New technology and later stage companies need the kind of investing that VCs offer.

Angel Investors are usually high net worth individuals, many times successful Entrepreneurs themselves, wanting to help other Entrepreneurs succeed and get a return on their investment. Angel's typical investment is in the range of \$50, 000 to \$1 million dollars.

Angel investors are much like a partner- the Entrepreneur gives up part of the ownership of the firm in exchange for cash and the business expertise and connections that the Angel brings in.

Sounds great, but finding Angels or Angels finding good firms to fund are both extremely difficult.

Angels are usually very busy anyway and constantly bombarded with requests, so it is impossible to sift through all the clutter to determine what warrants attention. So... most of the time none get attention.

On the other hand, really good business ideas that Angels are interested in are also rare. Investors are not interested in lifestyle businesses, or businesses that are really just a job for the Entrepreneur. The kind of businesses investors are interested in have obvious growth potential and are not dependent on the Entrepreneur to do all the work.

Getting the two together... Angels and “good” business ideas... should be a major Economic Development activity. An organized Angel Network focused on area Entrepreneurs could have amazing long term effects. If just a portion of the local money invested elsewhere were pumped into the local Entrepreneurial spirit to develop local businesses, a progressive economy would become a world-class economy right before our eyes.