

# Angel Metrics

---

By Michael R. D'Angelo (mdangelo@alum.mit.edu)

Nowadays we hear a great number of stories involving troubled portfolio companies - tales of high burn, delayed product introductions, markets which didn't mature, down-rounds, survival rounds, and the occasional wind down. Still, despite the realities of these highly publicized struggles, there is evidence suggesting that angels are continuing to invest in young, promising companies. While angels have become more selective and engage a more rigorous analysis of the prospect company, they are still investing.

Based on the lessons learned during our Series A round, we have crafted a fund raising strategy based on a number of clearly defined successive steps that are governed by metrics. The strategy is designed to efficiently identify prospective angel leads and bring them to a successful close in a timely manner. Our strategy benefits not only the entrepreneur but also enables individual angels to more efficiently process deal leads as they are encountered.

Implicit in our strategy is the realization that new angel leads possess a finite useful life. Lexent's Chairman, Bard Salmon, refers to this empirical observation as the angel lead life cycle. Following initial contact with a prospective investor, there is a window of opportunity that occurs in four to five weeks where the statistical likelihood of closing is at its maximum. Following this period, a successful close is less and less likely, until it ultimately falls toward zero in the six to eight weeks following the first meaningful contact. All activities leading up to the optimum window must be carefully orchestrated, with the frequency of contact and information flow suitably timed to enable a positive investment decision at point of peak probability of closure. The concept is empirical – the collective result of many millions of dollars in angel capital raised, in both good times and bad.

Starting with the probability curve governing the frequency of contact and flow of information, we use a funnel strategy to efficiently sift through the angel leads we generate, minimizing the degree to which we might otherwise waste valuable time chasing down unlikely prospects. The successive funnel levels are [1] name generation, [2] first encounter, [3] delivery/review of the executive summary, [4] meeting(s), [5] subscription and [6] the final step of a check cleared and money banked. Effort is made to ensure that each level in the angel lead funnel is appropriately balanced to feed the next, allowing decisions to be reached in a natural manner, without force, at the point of peak probability of closure.

Preparation is key to the successful implementation of the angel funnel strategy, increasing the likelihood that an angel lead is brought through the funnel to a successful close. Preparation involves the collection of documents concisely describing the company and a clear articulation of the financing structure. For Lexent, it means an extended executive summary with supporting appendices on the people, product, market, capital requirements and revenue growth. Within this descriptive material we focus on three key areas: the demonstration of customer acceptance of our technology, the demonstration of an internal understanding of the resources required to become cash flow positive, and the demonstration that we have a product that addresses a clearly defined market need. Tom Black, one of Lexent's early investors, likes to think of any company as a 3-legged stool: product, sales, and financing. Tom explains that in addition to demonstrating a thorough understanding of capital needs and sales strategies, it is critically important for entrepreneurs to show

they have a product that solves a clearly defined problem - this allows an investor the opportunity to say, "oh yeah, I can see how that product would be attractive."

On the legal end, under the guidance of Gerald Kehoe at Bingham Dana we generated a set of documents including a two-page term sheet, subscription agreement, note purchase agreement, convertible note, shareholder/board votes and the charter amendment authorizing the Series A preferred stock. Taking place in the background is preparatory work for the filing of the SEC Form D's which need to occur in a timely manner as capital flows in. The overall process is one of defining the amount of financing, the application of proceeds, the form of the financing, the company valuation, the form of incentive offerings, the sourcing of leads and the timeframe.

Lead generation is a critical step. We must feed the funnel. The best source of leads has turned out to be our current investors. Second to our current investors are people known to the company. Third are network events where angels are known to gather, giving preference to those events hosted by an institution or group for which one or more of our team is affiliated - MIT's Technology Capital Network is an example. Beyond these there are diminishing returns. It is safe to say that reliance on the random encounter will yield a long wait.

Accelerating the close can be accomplished with an incentive offering to those angels who move quickly to close. The incentive comes in the form of what we call a dissolving discount - at its maximum at the start of the round and timed to dissolve as the round comes to a close, ultimately uncovering the true value of the company. To implement the discount we structure a debt financing with mandatory conversion to preferred stock. Each investor is given a discount on the conversion price to preferred stock depending on the timing of the close.

Fund raising is time consuming and requires a dedicated person to lead the effort. Ideally it is a full time job. Unfortunately, few of us have the luxury of dedicating ourselves full time to the fund raising effort since we have a business to run. Begin with an outstanding business opportunity and treat the process systematically and honestly. The operative word not to lose sight of is "go" - get out of the office, nothing happens behind your desk. Plan wisely and above all, don't run out of CASH.

Michael R. D'Angelo (mdangelo@alum.mit.edu) is founder and CEO of Lexent Technologies, Inc. (www.lexent.com), a Lexington based early stage company that designs, markets and manufactures wireless IT security solutions for laptop PC's.