



A Profile of Bank Angel Investors

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Profile of Bank Angel Investors

- ✔ Study Design
- ✔ General Angel Investor Data
- ✔ Bank Angel Profile
 - Demographics
 - Deal Characteristics
 - Investment Process
 - Investment Motivations
- ✔ Findings & Implications
- ✔ Future Research



Study Design

- ✔ Objective: Develop a profile of angel investors that found new banks
- ✔ Motivation/Relevance:
 - Primary: Augment angel investor knowledge base using large/accessible data set (bank founders)
 - Secondary: Increase understanding of new bank phenomenon
- ✔ Methodology: Mixed Methods
 - Quantitative: Mailed-out survey
 - Qualitative: Interviews



Study Design

✓ Survey

- 4000 surveys mailed to every independent bank (n=325) founded in 2001 & 2002 (last two complete years at time of study design)
- Source: FDIC online database
- 330 responses
 - Broad representation: 109 banks in 33 states
 - 221 from non-employee directors/founders
 - 109 from employee founders (typically CEO)
 - Employee responses were not focus of this study; set aside for future research

✓ Interviews

- 21 open ended interviews
- Source: Contacts developed during research
- 11 de novo bank founders; 10 advisors to de novo bank founders (accountants, lawyers, investment bankers, etc.)
- Very helpful on subtle motivational issues



Key General Angel Studies Cited

- ✔ Bank Angel data was reported with general angel data as context (statistical testing between two groups was not objective of study).
- ✔ General angel investor profile compiled in Morrissette (2005) using data primarily from:
 - Gaston (1989)
 - Freear, Sohl & Wetzel (1990, 1992, 1993, 1994)
 - Hill & Power (2002)
 - Sullivan & Miller (1990, 1996)
 - Benjamin & Margulis (2001)
 - Van Osnabrugge (2000)
- ✔ See Exhibits 3 & 4



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Angel Investing Defined

- ✔ Angel investors provide capital to start-up companies
- ✔ Angels are one of three primary sources of new venture funding (Founder/Friends/Family, Angels, Venture Capital)
- ✔ Sometimes called *informal investors*, *private investors*, or *business angels*
- ✔ Term is derived from financial backers of theatrical productions (plays, operas, etc.) that are also called *angels*.
- ✔ Not a new dot-com phenomenon
 - Dates back to 13th century (in Marco Polo's time angels got 75% of profit; entrepreneur 25%)
 - Henry Ford had 5 angels that invested \$41,500; 15 years later their investment was worth \$145 million



Angels are... (*typically*) ...

- ✔ middle-aged, successful, somewhat wealthy entrepreneurs
- ✔ willing to invest in start-up companies seeking good return on their investment
- ✔ but also motivated by non-financial benefits such as the exhilaration of helping create another enterprise.

Angel Investing Statistics

Number of Angels Investing Each Year		
	400,000	Benjamin & Margulis (2001, p 3 & p. 20)
	400,000	Timmons & Spinelli (2004, p. 472)
	300,000	Van Osnabrugge & Robinson (2000, p. 68)
	220,000	Sohl (2004, p. 1)
	300,000	Wetzel and Freear (1998)

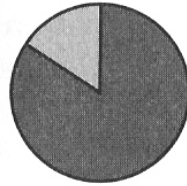
Number of Deals per Year		
	60,000	Van Osnabrugge & Robinson (2000, p. 68)
	50,000	Sohl (2003)
	50,000	Hill & Power (2002, p. 26)
	140,000	Benjamin & Margulis (2001, p. 2)

Amount of Investment per Year		
	\$40-60 billion	Benjamin & Margulis (2001, p. 2 and p. 20)
	\$30 billion	Timmons & Spinelli (2004, p. 471)
	\$50-60 billion	Van Osnabrugge & Robinson (2000, p. 69)
	\$100 billion	NCVA, Cullen (1998)
	\$40 billion	Sohl (2003)
	\$18 billion in 2003	Sohl (2004, p. 1)
	\$40 billion	Hill & Power (2002, p. 26)
	\$50-60 billion	Benjamin & Margulis (1996)

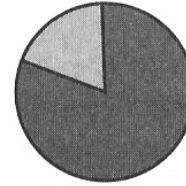
Comparison to VCs

Comparative Size of Angel and Venture Capital Markets

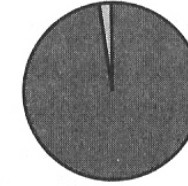
Comparative Size
of Investment
Portfolios
(Ratio 5:1)



Comparative Size
of Amounts
Invested Annually
(Ratio 3.5:1)



Comparative Number
of Entrepreneurial
Firms Funded Annually
(Ratio 30:1 or 40:1)



■ Angels ■ VCs

Source: Van Osnabrugge & Robinson (2000, p 69)

Comparison to VCs

"Angels invest their own money; VCs invest other people's money."

Hill & Power
2002

Differences between Business Angels and Venture Capitalists

	Business Angels	Venture Capital
Funding Source	Angel's own money	Investors
Number of deals per year	1 every 2 years	5-10 per year
Typical investment per company	\$25-250,000; average \$50-75,000	\$1-10 million; average of \$4 mil
Company Stage	Small, start-up, early stage	Larger, expansion stage
Geographic Focus	Usually near (within 1-2 hours) of home	Usually nationwide, sometimes regional
Industry Focus	No focus, but prefer industries they know	Often focus on 1-2 industries
Source of deals	Other angels, friends, business contacts	Proposals submitted, other VCs
Decision Maker	Individual, experienced entrepreneur, personal, 50 years old	Professional, MBAs, committees, 40 year olds
Analysis/Due Diligence	Minimal, informal, subjective, judgment	Extensive, formal, analytical, spreadsheets
Investment Structure	Simple, common stock	Complex, Convertible Preferred Stock
Involvement	Hands-on	Strategic, Board Seat
Investment Time/Horizon	Longer, 5 or more years	Shorter 3-5 years
Exit/Harvest Strategy	Less important, long-term investment horizon	Important, IPO or Sell Company
Return on Investment Expectations	20-30% but often don't have predetermined ROI expectation	Expect 30-50% ROI

Sources: Van Osnabrugge & Robinson (2000, pp.106-111), Benjamin & Margulis (2001, pp 32-33); Hill & Power (2002, pp. 24-26, 61-67, 249), National Venture Capital Association website at www.ncva.org, Gaston (1989, pp. 14-27, 44-78), Freear, Sohl and Wetzel (1994).



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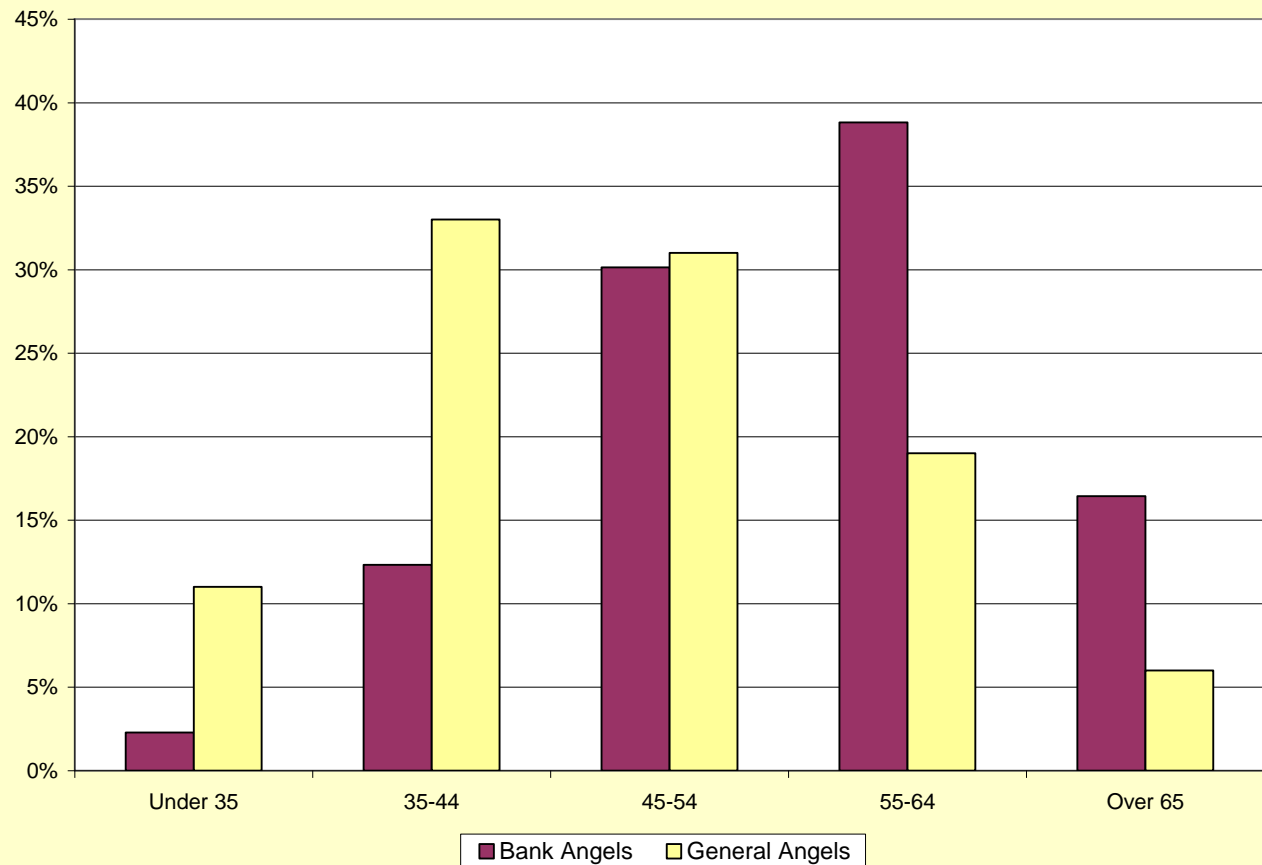


Demographics

Characteristic	General Angel	Bank Angel
<i>Demographic:</i>		
Age	47-50 years old	Older; average 55 years old; 55% are age 55 or older
Gender	85-95% male	96% male
Education	60-80% have college degree	Data not collected
Net Worth	Most over \$1 million	Much higher; average \$5 million; 87% worth \$1 million or more.
Business Background	70% own/manage a business; 83% have entrepreneurial experience	Similar; 86% own/have owned a company; 80% consider themselves entrepreneurs
General Angel Data Sources: Primary sources are Gaston (1989); Freear, Sohl & Wetzel (1990, 1992, 1993, 1994), Hill & Power (2002), Sullivan & Miller (1990, 1996), and Benjamin & Margulis (2001).		

Demographics

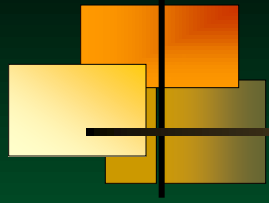
Angel Investors by Age Group



General Angel Data Source: Gaston (1989, p. 18)

Bank
Angels
are
older;
why?

Demographics



Angel Investors Net Worth

	Bank Angels	Angels Overall
Under \$500,000	3%	39%
\$500 - \$ 1 million	10%	24%
\$1 – 3 million	29%	37% (*55%)
\$3 – 5 million	23%	
\$5 – 10 million	16%	
Over \$10 million	19%	

General Angel Data Source: Gaston (1989, p. 19)

*adjusted for inflation

87% of
Bank Angels
Are Worth
>\$ 1 mil

Deal Characteristics

Bank Angels
Invest Much
More

Characteristic	General Angel	Bank Angel
<i>Deal Characteristics:</i>		
Investment Size	Average is \$50-75,000; 85% is under \$250,000	Much higher. Average over \$250,000; 41% over \$250,000
Frequency	1 deal every 18-24 months	Not applicable
Geography	Close to home (75-85% within 50 miles of home)	Data not collected
Industry	Eclectic; prefer industries they know; manufacturing most common	Not applicable
Company Stage	Most invest during formation or in company less than 2 years old	Data were all new firms (new banks)
General Angel Data Sources: Primary sources are Gaston (1989); Freear, Sohl & Wetzel (1990, 1992, 1993, 1994), Hill & Power (2002), Sullivan & Miller (1990, 1996), and Benjamin & Margulis (2001).		

Investment Process

Characteristic	General Angel	Bank Angel
<i>Investment Process:</i>		
Sourcing	Friends and business associates	Data not collected
Co-Investing	Not invest alone; 80-90% of deals have multiple angels	Not applicable; all banks in data set had multiple investors
Due Diligence	Informal, subjective, focus on entrepreneur	Data not collected
Contract Structure	80% of deals are simple common stock structure	Data not collected
Role/Involvement	Hands on; meet or talk with entrepreneur several times each month; full or part-time employee 40% of the time	Sample was bank directors; all were involved.
ROI Expectations	Most expect 25-30%	Much lower. Expect 11-12%; 53% expect 10% or less.
Holding Period	Average is 5 years	Much longer. 52% plan to hold more than 10 years.
Investment Criteria	Focus on quality of the entrepreneur	Data not collected.
Non-financial	Thrill/fun of helping start a new company significant motivation for most angels	Community service and excitement more important than ROI. Closer to Sullivan's altruistic or hedonistic clusters.
General Angel Data Sources: Primary sources are Gaston (1989); Freear, Sohl & Wetzel (1990, 1992, 1993, 1994), Hill & Power (2002), Sullivan & Miller (1990, 1996), and Benjamin & Margulis (2001).		

Very different



ROI & Holding Period Expectations Very Different

Clearly Bank
Angel
Investments
are different.
Why?

Motivation
data provides
insight.

- ▼ ROI:30% (vs Bank Angel 11%)
 - 34% (Hill & Power, 2002, p. 238)
 - 30% (Benjamin & Margulis, 2001, p. 23)
 - 32% (Freear Sohl & Wetzel, 1995, p. 91)
 - 32% (Linde & Prasad, 2000, p. 48)
 - 28% (Sullivan & Miller, 1990, p. 302)
 - 25% (Gaston, 1989, p. 44)
 - 33% for repeat angels (Van Osnabrugge, 1998, p. 36)

- ▼ Holding Period: 5 years (vs Bank Angel 11 yrs)
 - 4.8 years (Freear, Sohl & Wetzel, 1995, p. 92)
 - 4 years (Linde & Prasad, 2000)
 - 5-6 years (Van Osnabrugge, 1998, p. 38)
 - 5-7 years (Hoontrakul, 2001)
 - 5.1 years (Gaston, 1989, p. 45)
 - 8 year (Benjamin & Margulis, 2001, p. 254)



Investment Motivations

- ▼ Data was collected on motivation in four areas:
 1. Return on Investment (ROI)
 2. Risk
 3. Other financial benefits
 4. Non-Financial benefits



Investment Motivations: ROI

- ✓ Average expected ROI of 11% from bank angel investments (vs 30% for general angel)
- ✓ The difference is the investment not the investor:
 - Half of bank angel investors surveyed also do other angel investing in non-banks (which allows robust comparisons between bank angel investments and non-bank angel investments)
 - Expected return by bank angels on non-bank investments is 21%, very similar to general angel studies
- ✓ Lower required return could be due to:
 - Lower perceived risk
 - Other non-ROI financial benefits
 - Non-financial benefits



Investment Motivations: Risk

- ✓ Bank Angels perceive less risk in bank investment than in other angel investments
 - Bank Angel Investments
 - On average, respondents rated bank angel investment risk to be equal to S&P 500 mutual fund
 - Over half rated it LESS risky than an S&P mutual fund investment
 - Non-Bank Angel Investments
 - On average bank angels said that their non-bank investments had 1.5-2x the risk of the S&P
 - Over 40% said these investments had 2x or more risk than the S&P
 - Data appears to indicate that bank angel investors see bank investments as different (less risky) and does not indicate a risk-underestimation problem (see Maula, Autio & Arenius, 2003)



Investment Motivations: Other Non-ROI Financial Benefits

- ✓ Data showed no evidence of motivation from other financial benefits
 - Ex. Insurance agent on bank board would see opportunity to sell insurance to bank or bank clients
- ✓ Of note: bank regulations strictly prohibit self-dealing by bank directors; a strong disincentive.

Investment Motivations: Non-Financial Benefits

- ✓ General angels studies have found non-financial benefits are a significant factor:
 - Freear, Sohl & Wetzel (1995) found that 50% of angels accept lower returns because part of their return is psychic income such as creation of jobs in the community or the satisfaction of helping another entrepreneur succeed.
 - Sullivan (1991) found that for one-third of angel investors return on investment was not their primary motivation

Sullivan & Miller (1990)	
Non-financial benefit	% willing to give-up financial return to obtain benefit
Socially beneficial product	83%
Fun to be a part of the company	66%
Creation of local jobs	65%
Firm nearby vs. 300 miles away	63%
Interacting with highly regarded investors	61%
Company committed to social ideals you support	59%
Exciting investment	47%

Linde & Prasad (2000)	
Non-Financial Reasons	Percent
Desire to "Give Back"	60%
Enjoy Involvement	56%
Networking	28%
Other	44%
Stay Up-to-date	24%
Challenge	24%



Investment Motivations: Non-Financial Benefits

- ✔ Bank angel data is consistent with general angel findings on non-financial benefits.
- ✔ Top 5 reasons for bank angel investments:
 - Community need (48%)
 - ROI (36%)
 - Excitement of new venture (33%)
 - Serving on bank board (30%)
 - Fun/enjoyment (21%)
- ✔ Interview respondents similar. Top three reasons:
 - Community need (80%)
 - ROI (80%)
 - Bank director (60%)



Investment Motivations: Non-Financial Benefits

Sullivan & Miller (1996) study segmented angels into three types or clusters

- ✓ Economic Investor: (47% of total)
 - Financial motivations are very important
 - Highest ROI expectations (30% versus 21% for hedonistic)
 - Perceives more risk than other clusters (2-3x)
- ✓ Hedonistic Investor (31% of total)
 - Emphasis on enjoyment aspects of investing (enjoys entrepreneurial process, enjoys fun of interesting investment)
 - Lowest ROI expectations (21% versus 30% economic)
 - More likely to invest with a group
- ✓ Altruistic Investor (22% of total)
 - See value in supporting new business and/or socially beneficial product
 - More patient investors (longest holding period - 7 years)

While my study did not test to apply these clusters to bank angel investors, my interpretation of the data is that bank angels have a higher occurrence in the hedonistic and altruistic clusters (see Exhibit 2).



Findings & Implications

- ✔ Bank angels are very similar to general angel investors
- ✔ Bank angels aren't very different, but bank angel investments are. Less perceived risk and more emphasis on non-financial benefits.
- ✔ Bank angels are wealthy/successful (net worth avg \$5 mil), experienced entrepreneurs that are committed to the new venture (involved and with an average investment over \$250,000); this bodes well for success of new venture



Future Research

- ✔ Test if Sullivan & Miller clusters vary by industry or deal type
- ✔ Explore risk and return perceptions of angels (risk underestimation hypothesis)
- ✔ Banking policy implications (test correlations between angel characteristics and bank success/failure)
- ✔ Application of franchising theory to new bank start-ups

Exhibit 1: Bank Angel Profile

Exhibit 1: Summary of Bank Angel Investor Characteristics

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<i>Demographic:</i>		
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Exhibit 2: Compare to Sullivan & Miller

Exhibit 2: Comparing Sullivan & Miller Clusters to Bank Angel Survey Results

Sullivan & Miller Cluster Characteristics	Consistency*	Related Bank Angel Survey Results
<i>*Consistency denotes consistency between bank angel data and Sullivan & Miller clusters.</i>		
Economic Investor: (47% of total)	Low	
Only financial motivations are important	Low	Non-financial motivations are very important; ROI ranked below community need and fun/excitement
Highest ROI expectations (30% versus 21% for hedonistic)	Low	Much lower ROI expectation (11-12%)
Perceives more risk than other clusters (2-3x)	Low	Perceives less risk than average
Largest average investment	High	Bank angels have very large average investment (over \$250k)
Hedonistic Investor (31% of total)	High	
Emphasis on enjoyment aspects of investing (enjoys entrepreneurial process, enjoys fun of interesting investment)	High	Enjoyment/fun/excitement second most important investment factor
Lowest ROI expectations (21% versus 30% economic)	High	Low ROI expectation (11-12%)
More likely to invest with a group	High	Average size of founder group is 10 versus 2-3 for general angels
Slightly older than other clusters	High	Bank angels average age is 55 versus 50 for general angels
Altruistic Investor (22% of total)	High	
See value in supporting new business and/or socially beneficial product	High	Community need most important highest investment
More patient investors (longest holding period - 7 years)	High	Average holding period of 11 years
Average investment smaller	Low	Bank angels have very large average investment (over \$250k)

Source: Sullivan & Miller, 1996; Morrissette, 2005.

Exhibit 3: Angel Literature

Exhibit 3 Primary Sources of General Angel Investor Characteristics			
Authors	Date	Sample Size	Comment
Maula, Autio & Arenius	2003	6007 adults in Finland	Excellent theory-testing research using international data; extensive up-to-date literature review;
Hill & Power	2002	50	More anecdotal than statistical
Benjamin & Margulis	2001	n/a	Proprietary, only partial data published; would not provide full tabulation when requested
Amis & Stevenson	2001	50	Excellent survey of angel investor best practices
Van Osnabrugge & Robinson	2000	Mostly literature review, primary data on 70 Angel matching services	Comprehensive review of literature, little or no primary data
Sullivan & Miller	1996	214	Insightful work segmenting angels into three investor types (economic, hedonistic, altruistic).
Duxbury, Haines & Riding	1996	279 (Canada)	Thorough study of psychological attributes of angels
Freear, Sohl and Wetzel	1994 & 1992	184	Compares angels with non-angels
Freear, Sohl and Wetzel	1993	409	Seven year longitudinal survey of members of an investor matching network (1985-1992). Found demographic data consistent with other studies. Found investor behavior relatively constant over time.
Sullivan	1991	210	Found angels who are/were entrepreneurs perceive less downside risk in start-ups than do other angel investors
Sullivan & Miller	1990	214	Interesting study which tests if two aspects of finance theory (risk/return tradeoff and wealth-maximization objective) hold for angels
Freear, Sohl & Wetzel	1990	284	Studied investors in new technology firms
Gaston	1989	435	Extensive profile of angel investor characteristics including breakouts by angel subtypes.
Wetzel	1983	n/a	Considered the first/founding study of angel investors; the stream of angel investor literature begins here.

Exhibit 4: General Angel Profile

Exhibit 4 Summary of General Angel Investor Characteristics

Demographics:

Age	47-50 years old
Gender	85-95% male
Education	60-80% have college degree
Net Worth	Most over \$1 million
Business Background	70% own/manage a business; 83% have entrepreneurial experience

Deal Characteristics:

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