

Business Angels – A Subspecies of the *homo oeconomicus ludens*

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Abstract: Business Angels invest in start-up companies in their early stage. This type of investor usually has a good knowledge of the start-up's industry sector, and in addition to the funds he invests, his management experience and his network can be useful for start-ups. Business Angel involvement has shown to improve the success rate and the profitability of start-ups. The article depicts the relationship between entrepreneurs and Business Angels in four case examples.

Keywords: Business Angel · Early stage · Investment · Start-up

The Prototypical Business Angel

Business Angels are individuals who invest in start-up companies. The prototypical Business Angel may have built a company himself, experienced roadblocks on his way, surmounted them, and increased the value of the company with prudent management combined with bold moves, until he was approached by a larger enterprise that saw his company as a strategic addition to its activities.

He agreed to sell his company and found himself with a substantial amount of money. After a prolonged holiday, sailing the Aegean Sea, driving classic cars, or cutting his lawn, he found he missed some business action.

During this time he was approached by a former employee, met him for lunch and was presented with a plan to develop a product and start a company. As the project was positioned in an industry sector he knew so well, he was rather enticed.

He was not interested in managing a company anymore, he didn't want to do research and development himself, he had no

qualms about being in the background. All he was interested in was being involved, feeling the pulse of the times, sharing the excitement of young entrepreneurs and helping out with money and advice.

So he checked up the opportunity closely, and after further discussions he decided to swap the equivalent of a vintage sports car for some equity in the newly founded start-up. The sum injected was a substantial amount for the company to get going, and on the other hand an amount he could afford to write off in case of failure.

While assessing this case, he had contacted a few former business partners and they too were ready to invest. One of them was a recently retired scientist he consulted on the specifics of the project, another one was a dentist with a knack for technology, a third one was a manager in a listed company who was ready to add to the funds as he saw the potential of the company to be sold at a multiple if the product would be successful in a few years.

Our unnamed prototypical Business Angel, apart from investing, also took a seat on the board of the new company, representing the interests of the investors. Moreover, the newly minted entrepreneurs valued having his management experience with SMEs on board.

Sure enough, the word spread, and soon the investors were approached by other young entrepreneurs in search of funds for projects.

A few years later they found themselves with a portfolio of investments of CHF 100 to 400k for each project. Furthermore, they had joined one of the clubs that aggregate interested investors.

While Business Angels are glad to invest in promising projects, it is no walk in the park for a person with a project to find and convince investors. A good idea and a solid scientific background will not do on their own.

Case Example: Creoptix

It took Kaspar Cottier a few years to develop his hunch to a business idea that finally became Creoptix.

When Kaspar Cottier worked on his thesis on optical waveguides, he was fascinated by the physics of the topic. During discussions with colleagues, the technical possibilities emerged which led to further research on label-free waveguide grating sensors. Upon finishing his thesis he started to work as an optics engineer in a Swiss small and medium-sized enterprise (SME), following a career in supply chain and process engineering. At the same time, however, and while filing patents for the company, he followed up on his original topic until he was ready to go his own way. He was aware that his own money and the support of the family were valuable and important, but this initial money would not be enough for a company. Further funds would be necessary on the way.

Meanwhile, Cottier had managed to obtain a Commission for Technology and Innovation (CTI) grant to prove the concept and to build a prototype. While working on the prototype, Cottier wrote his business plan. Realizing a one-man show would not satisfy investors, he jumped on the opportunity when his CTI coach suggested to team up with Matyas Vegh, a biologist experienced with start-ups. As Cottier's penchant is for technology, the preference of Vegh for management and sales made for a perfect match.

Together, they got on the road and started touring investors, presenting their project, while still living on their own savings. They presented, discussed, honed the plan, and they learned the hard way. "There was this presentation in Frankfurt," Vegh says, "when the potential investor tore our plan to pieces. However, when we sat on the train back to Zurich, we realized the

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investor was right. We had to rethink our business model.” With their new model, they approached other investors, as well as Business Angel clubs.

While some Business Angels prefer to act on their own, others are organized in clubs offering a platform for companies to present and for Business Angels to invest and co-invest, thus aggregating investments and allowing for projects with higher capital needs, usually up to CHF 2 or 3 million. In these clubs, each investor invests individually, and one of them will act as a Lead Investor dealing directly with the company, while also representing the co-investors. Apart from such clubs, there also exist associations set up as businesses, where investors inject funds for collective investments managed by this association.

With their new plan, Cottier and Vegh eventually were invited to pitch for 10 minutes at a StartAngels Network reunion. The response was rather enthusiastic, an intense meeting with interested members followed shortly afterwards. The Lead Investor initiated the due diligence test, a term sheet balancing the interests of investors and entrepreneurs was negotiated and finalized, and the deal was closed within some three months, which represents a comparably short time. It did help that the valuation of the company expected by Cottier and Vegh was reasonable, valuation being the basis for the expected return on the investment.

Contrary to their label, Business Angels do not forward monies *à fonds perdu*. They are businessmen, they want a return on their investment, and with the investment being risky, they expect the return to be a comfortable multiple of the sum invested. This is perfectly rational, as few businesses succeed, some survive, and about half of them will end up a total loss. Furthermore, the funds invested are illiquid for years, sometimes only 4 to 5 years, but usually for much longer periods. To spread the risks, Business Angels thus will invest in a portfolio of companies, usually some 10, 12 or more.

Apart from the return on their investment, Business Angels are motivated by their bent for technology and science, by the interest of having the finger on the pulse in their field of interest, by the prospect of meeting innovative personalities, and by the sheer joy (or delusion) of shaping the future.

Currently, two members of StartAngels sit on the board of Creoptix, and others can lend a helping hand. “When a supplier”, explains Vegh, “postponed the delivery of a critical component – jeopardizing the success and burning funds – one of the other members helped by introducing us to the supplier’s senior management, whereupon the issue was solved – our delivery was prioritized.”

Case Example: credentis and the Development of Curodont Repair

Working as a scientist in industry, Dominik Lysek came across a British research project on self-assembling peptides to regenerate bone material. He saw that this concept had the potential to be used on teeth as well, thus allowing a new way to treat caries. He initially moved on to work for another company. Two years later, though, he still had this project on his mind, so he contacted the scientists at Leeds University. Sure enough, they had patented the process and what’s more, they were ready to licence the patent to him. He cut his fulltime job in industry to 50%, started working on his business plan, arranged for specific experiments with the UK team and set out looking for investors. Lysek was lucky to have a boss who supported his entrepreneurial endeavours, and helped him find the initial contacts, and the first interested investors. Nevertheless, it took him 1.5 years and presentations at organisations like Novartis Venture Fund, Venture kick, BioBAC, and StartAngels Network until he was able to raise the funds necessary from the angel groups to start credentis ag and the development of Curodont Repair.

“A start-up entrepreneur has a vision, not a steady revenues stream – this does not fit into the classic risk approach banks take when evaluating loans”, says Lysek. “You therefore need Business Angels who share your vision and trust in your abilities to make it a reality. Some Business Angels will know the industry you’re in, or some aspects of it, while others will just trust you and their Lead Investor.”

“Trust is essential in this relationship between Business Angels and entrepreneurs”, Lysek continues. “My lead investor told me at a very early stage: the moment I doubt your trustworthiness I will leave the discussions. And he is right. Honesty is crucial.”

In the meantime, credentis has changed market approach and business model as the market seems to take more effort than first expected. Luckily, further research and development using the original knowhow led to several additional products based on credentis’ Curolox® Technology. This includes professional and OTC dental products, offering a path to multiple industry partnerships and revenue streams.

In Lysek’s view, “Business Angels are motivated by a penchant for innovation and technology, and they also want to make money.”

“Business Angels will not always agree with you, and they will have a different view based on their personal background, but the ensuing discussions are fruitful and prevent you from seeing things in too rosy a light.”

Case Example: Piquar

Vladimir Cmiljanovic got into PI3k research at the end of his Bachelor, subsequently working on chemical antibodies and identifying the possibility to create a drug for treating cancer. He followed up on this idea with his thesis and managed to secure a grant from Novartis to do the proof of concept on mice. Pursuing this line in a Postdoctorate, with the help of foundations securing the funds, he reached the crossroads to either follow an academic career or to start his own company. Having learned about entrepreneurship from the cradle, being born to a father who supplied the automotive industry with chemicals, it is not surprising Cmiljanovic chose the entrepreneurial route.

Looking for partners and funds he soon realized he was at a too early stage for Business Angels, but he persevered and managed to motivate a number of drug specialists he had got to know in the course of his research to invest individually and to actually join his efforts. He then was able to attract individual Business Angels and subsequently to raise CHF 2.5M seed money.

“I did write a business plan in 2010”, Cmiljanovic says, “but I rarely had to forward it. The company presentation usually was the start of the discussions, while the business plan proved important as an exercise to clarify the business to myself. Of course, it developed over the years with each discussion.”

Continually expanding the number of investors, by 2013, he managed to convince a VC with substantial knowhow in oncology to join and invest. VCs, short for Venture Capitalists, tend to raise larger sums than Business Angels and to invest in later stages than Business Angels. Furthermore, Business Angels invest their own money, while VCs (and banks) invest funds entrusted to them. At this time, collaborations of VCs and Angels are infrequent, but the two worlds are converging: Angels are increasingly professionalizing their investment activities, and VCs need pipelines of Start-ups.

Cmiljanovic attributes the success of Piquar to the whole of his investors, partners, and co-workers. “You are not successful on your own,” he says. “Having been active in team sports, in handball, I know that success always is the result of the coordinated effort of people working together.”

Case Example: BioVersys

When Marc Gitzinger started working on his thesis, he also booked a course on Founding Your Own Company – just

to do something non-scientific. However, the route from bacterial gene regulation to a viable business idea was a long and winding road rather than a race track. After many a discussion of ideas, concepts, inklings and hypotheses with colleagues, friends and professors he came to the conclusion that resistance to antibiotics would be a most promising avenue to travel, as he saw possibilities to switch off resistance in bacteria, thus re-enabling the use of known antibiotics.

Obtaining funds from CTI allowed for a proof of concept on the topic of tuberculosis. At the same time, Gitzinger managed to attract attention to his concept and business idea with the help of prize competitions such as Venture Kick.

“It is essential that you can explain your project clearly in a few minutes”, Gitzinger says. “And if you can explain it to your grandmother, you probably passed the test for clarity and conciseness.” Investors and Business Angels often hear several company presentations in a row at an investment event, so it is crucial to get your message across easy and clear during this first chance.

The concept of Gitzinger’s team convinced BioBAC and EVA, and he was able

to raise seed money of some CHF 2.5M in 2010 for BioVersys. For the ensuing A investment round allowing the next steps of development, some CHF 9M were needed. While this represents a sum typically raised from VCs, Marc Gitzinger and his team finally managed to raise all the funds from individual Business Angels, Business Angel associations, banks and family offices. To gain access to the latter, Gitzinger explains, he was greatly helped by Business Angels paving the way and opening doors for him. “Business Angels have a distinctive motivation”, he says, “to actively support a company with their own expertise, experience and using their network.”

Business Angels in Switzerland

It might be worth mentioning that the active Business Angel involvement tends to improve the chances of survival, as well as the growth rate of start-up companies. Furthermore, Business Angels engagements are recognized to have a beneficial impact on innovation, job creation, and thus on the national economy.

For Life Sciences, a specialized Swiss Business Angels club is BioBAC (www.biobac.ch). This association finances projects independent of the geographical origin, while projects in the Basel area and in Switzerland in general are prioritized.

The StartAngels Network (www.startangels.ch) on the other hand only finances companies based in Switzerland. While regularly investing in Life Sciences companies, this club also finances companies in other industries ranging from ICT, electronics, micro and nano technologies, to cleantech.

Furthermore, Business Angels Switzerland (www.businessangels.ch) is present both in the French speaking and in the German speaking parts of Switzerland. This association invests in an again wider range of industries.

These associations hold regular meetings with presentations of companies, the annual frequency ranging from up to 30 for the Business Angels Switzerland to 3 for the StartAngels Network. Processes for submission and selection are comparable. Details can be found on the respective websites.

Received: September 12, 2014

“ “ As a chemist I am fascinated by the molecular language, and it is my scientific interest to understand nature on a molecular level. If one is lucky, new compounds with exciting properties might be synthesized during research. My advice is: patent the discovery, find enthusiastic colleagues and start a company. This will augment your life and may serve your fellow citizens. ” ”

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