Do’s and Don'ts of Investing in Science and Tech Companies

Whether you’re a seasoned angel investor or a newbie, investing in hard-science and technology companies can be challenging. Many times these types of opportunities are hard to source and understand. Propel(x) is here to help you towards better, smarter science and technology angel investing. Let’s start with the basics - some simple dos and don’ts.

Do:

Go in with your eyes wide open

Angel investing is not for the faint of heart. It is risky. Often it is extremely illiquid, even less liquid than real estate. You are placing your money in the hands of a very early and unproven venture. And when it comes to science and technology startups, the timelines are long, and if there are returns to be had, they will be further down the line. If you think that any of these things would keep you up at night, angel investing is not for you.

Your own research

Make sure you have a grasp of the technology, the management team and the market. In your initial evaluation you should assess the following:

1. The management team: Make sure you are familiar with the people running the company. What are their backgrounds? Listen to any talks they have given on YouTube. Check them out on LinkedIn. Communicate directly with them. Talk to others who may know them. The best ideas only see the light of day when they are shepherded by a strong leadership team.
2. Is there a market for the product: Is this something that people would spend money on? How big is that market? A vast market is not required, but it should be reasonably sized – close to a billion dollars at minimum for a high risk venture.
3. Competition: What does the playing field look like? You want the field to be heavily tilted in favor of your possible investment. Lesser competition is better.
4. What does the company have that the competition does not have: IP? Trade secrets? Exclusive agreements? These are all barriers to entry. Higher entry barriers are better.
5. Company exit strategy: Doe the company have a reasonable plan for an exit? At the seed stage, “we’ll be going public” is not a reasonable plan for an exit.

If you understand these basics, then you're ready to dive deeper and conduct a full evaluation of the company, including financials, management, and understanding the intellectual property, which we'll cover in-depth in part 3 of this series.

Ask questions

No, seriously. Ask questions. Ask so many questions. Ask questions until you feel like a four-year-old whose favorite phrase is "why?" Then ask some more questions. When it comes down to it, the better informed you are about a company, the better your chances of being successful. If you'd like to see some key questions to ask, click here.

Understand the terms of the deal

This is relevant for any type of angel investing and while seemingly obvious, it is important that you understand the terms of the deal. The most common type of funding instruments are convertible notes. We've provided a primer on what to look for in a convertible note here. The second common form of funding is what is known as equity funding, where the company sells shares of stock (common or preferred). This type of funding is often raised after the initial seed round. In most cases, the original investors' convertible notes will mature to preferred stock. Preferred stock often has rights that the general common stock does not (such as liquidity preferences). We will be providing more in-depth details on assessing deal terms in part 4 of the series.

Understand how this investment matches your personal and business goals

Do you want to make the world a better place? Do you have a particular interest in finding early detection of specific diseases? Decide which type of companies you want to associate yourself with, and then go after the companies that match those ideals. You will also need to decide if you want to have more than a passive involvement in the company. Are there ways for you to work with and participate in the startup's journey? If not, you may want to consider investing elsewhere.

Don't:

Fall in love

Take it from us: tunnel vision is never twenty-twenty. While it is natural to be excited about any investment you make, it should not color your understanding of the company's strengths, weaknesses, and market risks. After all, strength in one area could mask weaknesses in another. And in the game of risk that is angel investing, one weakness can be fatal.

Follow others

Most angel investors don't angel invest based on other angels, as our recent survey showed. As an investor, you want to develop an independent point of view. Assessing the technology, speaking with the leaders, evaluating the marketing strategies--all of these are skills you need to have firmly secured in your back pocket before angel investing. Basically, make sure you're confident in your own ability to evaluate a company. That way you won't be tempted to follow your roommate from college who assures you that personalized laser guns are the next big thing.

Expect a quick payout

In the digital age, playing the waiting game is akin to a lost art. When you invest in a science and technology startup, you are truly investing in the future, and the timelines for these companies are longer than the usual messaging or food delivery apps. But patience is a virtue for a reason; especially when investing in companies that have the potential to have a global impact.

Invest if you feel uncomfortable

Our final piece of advice? Trust your instincts. You already know more than you think you do, and following your gut is arguably the best thing you can do when approaching a new investment opportunity. If you feel uncomfortable, especially after doing your research, then don't move forward.

Now you're one step closer to becoming a savvy investor in science and technology startups. Lookout for part 2 of the series where we'll cover how to discover quality science and technology investment opportunities.

Ready to see what Propel(x) has to offer and what investment opportunities are available? Join now!
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