'Angel' investors shifting away from startups

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AUSTIN, Texas (Dow Jones/AP) -- Angel investors may be getting cold feet.

Less than half, or 48 percent, of investments by ``angels'' -- wealthy individuals willing to place bets on nascent businesses before anyone else -- through the second quarter of this year went to companies at the seed or startup stage. The rest went to later-stage deals, according to a recent study by the University of New Hampshire's Center for Venture Research.

The figure has fallen from 59 percent in the same period of 2004, and from around 75 percent several years ago, and has been ``dropping pretty steadily,'' said Jeffrey Sohl, the center's director.

The University of New Hampshire study pegged overall angel investments through this year's first half at $11 billion, a figure Sohl said puts the pace of investment on track to meet the 2004 full-year total of $22.5 billion.

Angel investors still constitute the largest source of funding for seed and startup-stage companies, according to the study. But angels appear to be making an increasing amount of follow-on investments in their existing companies, as well as opting for post-seed, later-stage deals in new companies. Both strategies draw money from the traditional seed-stage sweet spot, which threatens the pace of new business and product innovation.

``If we lose that seed market, we're in deep trouble,'' Sohl said. ``The (entrepreneur) in the garage stays in the garage.''

Several factors are fueling the trends. For one, a well-documented shift among venture capitalists toward later-stage deals has forced angel investors to bridge the gap by coughing up more follow-on funding for their newly minted companies.

Meanwhile, Sohl thinks the proliferation of organized angel groups -- as opposed to angels acting individually or with a couple friends -- may favor later-stage deals. By Sohl's count, upwards of 140 formal angel groups now are active, compared with about a dozen a decade ago.

``Some of these (groups) may be pooling their money and morphing into funds,'' he said, meaning they have greater amounts to put to work and thus look for bigger deals.

Tarby Bryant, who runs a nine-year-old organization called Gathering of Angels that attempts to link entrepreneurs with early-stage investors, concurred that the increasing formalization of the angel process may have something to do with the trends.

``When four or five or more people get together, conservatism often rules, and that could favor later-stage'' deals, Bryant said. ``The wheels of democracy don't move as fast as the individual passions of an investor who has money.''

But Bryant considers the more relevant factor to be a rise in investment conservatism among angels overall, regardless of whether they're acting individually or in groups.

The upshot is a preference for companies or business plans that appear better prepared and fleshed out, he said, which often equates to later stage.

``People are taking more time (to analyze investments), versus the crazy years of '98 and '99, where they would just wave checks in the air and couldn't wait to get on the train,'' Bryant said.

But he doesn't view the change necessarily as a negative, nor he think it has reached the point where new entrepreneurs with good ideas can't get funding.

``If they are tenacious in their approach to the process, I think that there is money out there,'' Bryant said.

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