TIDAL RIVER

Seasoned Investor Mysty Rusk Has Been Advising Angel Investors and Startups for Decades. Here, the Founder of the Largest Angel Investor Conference in the U.S. Offers Her Hard-Won Advice.

Mysty Rusk knows a thing or two about angel investing. In addition to serving as executive director of the Free Enterprise Institute at the Knauss School of Business at the University of San Diego, Rusk founded the largest angel investment conference in the country. San Diego Angel Conference, which has an active group of about 100 accredited investors, provides hands-on education for entrepreneurs and accredited angel investors through a seven-month series of events and workshops that culminates in a one-day conference and pitch competition. SDAC's goal is to active new angel investors by providing a learn-by-doing environment. Writer Amy Hourigan caught up with Mysty as SDAC announced its six 2022 startup finalists to get her best advice.

Amy Hourigan: Hi, Mysty. Thanks for agreeing to answer our questions! Let's dive right in. As the founder of the largest angel investment conference in the country, you must see tons of great pitches. How do you help new angels evaluate them? Do you have a checklist of things you look for?

Mysty Rusk: It would be great if we had a checklist or a quick way to narrow the field. Our overarching goal is to activate angel investors. So, at the end of the day, we need to help each investor find the evaluation method that is right for him or her. That means we don't have a prescribed method. We also don't have a pre-screening process. Instead, we've collected a number of tools, checklists and the like that we share with our investors so they get exposure to different methods.

Over the years, we've had anywhere from 90 to 124 applications each cycle. We have a process for narrowing the number of applicants to about 60, then 24, then 12, then six. When we are down to the finalists, investors split into teams and spend five to six weeks in due diligence before we get to the finale and pick a winner.

AH: Interesting. How can angels go about evaluating industries to which they have no connection? Is that a bad idea?

MR: Well, by starting out industry- and stage-agnostic, we get very diverse applications. It's like comparing apples, oranges, tarantulas, and giraffes. We tend to attract investors that are equally diverse. With a pretty good size group of investors, we find that we usually have a broad swath of industry and functional knowledge. Additionally, between all of us we have a great network of experts we can call on if needed. Expertise cuts both directions. In some cases, an investor who knows the industry well can ask the really tough questions early in the process, which makes it tougher for those companies to advance compared to industries where we know less, and we don't discover things until much later in the process.

AR: Do you have tips for evaluating businesses at different stages? Do your criteria change?

MR: It's a balancing act that investors work through every cycle. Early-stage companies have more risks to mitigate, but there's a bigger upside for early investors. Later-stage companies have less risk but are often less lucrative. Here are a couple of tips: First, if you are investing in software, look for an increase in users, and an increase in sales that follows the "triple, triple, triple, double, double." You want to watch how long it takes for users, or sales, to increase. If the numbers increase quickly—monthly, quarterly, annually—then the growth trajectory is what we expect for a software company. Second, if you are investing in biotech and looking for a fast return, see if the company has an exit strategy—one that happens pre-clinically, or pre-commercialization—and regulatory mitigation of risk, predicated 510K for example. If you are investing in biotech and looking for a really big return and can afford to wait for an exit, look for companies that have a novel approach to a big problem, that have a revolutionary solution. Disruption, and big returns, only happen when the solution is better *and* faster *and* less expensive than the current solution.

AH: I read that you stopped asking for business plans and that you now focus on business models.

MR: That's true. We've been pushing startups and early-stage companies away from business plans for at least a decade. Business plans are awesome and incredible roadmaps and strategic documents for more mature businesses. They are also time consuming and finite. Startups and scaling companies are in a constant state of flux. Customer needs, product requirements, competition, and even the regulatory environment are changing, and early-stage companies need to stay flexible and responsive to these changes. Various business modeling tools—Lean Canvas, for example—give founders a concrete way to deal with the less-than-concrete landscape.

AH: What do you see in a pitch that gets you excited?

MR: I really like to see a founder who can nail the product–market fit quickly and spend most of the pitch talking through the go-to-market strategy, the business model, and how the use of funds will help de-risk the future and help the company start to scale. I don't think a founder can underestimate the value of a good competition slide and a timeline that shows how funding, product launches and other milestones fit together to tell the story.

On a personal note, I really get excited when a founder shares his or her moment of genius, and I get to fall into their discovery, see their passion and join them for a moment as they work to bring the dream to life.

AH: How important is it for an angel investor to have a network?

MR: The network is one of the most valuable assets an angel investor can develop. I've been doing this for nearly 20 years and still way too often meet a founder or see a pitch where I can't quite understand some of the finer points or potential risks. Having a great network is good for several reasons: (1) Investors pass deals around. I may see a deal that doesn't meet my criteria, or I can't invest in it for some other reason. If I see a good deal, I'll share it with other investors in my network that I know are interested—either in an industry, a problem they care about, a price point or expected timing on a return. (2) Investors lean on each other. There are a handful of industries, or functional areas, that any given investor feels comfortable with. If I see something interesting, I'll call someone in my network and ask for help deciphering the deal. People in my network call on me in the same way. (3) Investors invest together. The majority of investors, something like 80 percent, have a net worth of $5M. For those of us in that category, we're not really in a position to write $50K–$200K checks, and honestly, we don't want startups to have crazy cap tables loaded with small-volume investors. The legal structures have gotten so much better, and the costs have come down to assemble investors using instruments like the SPV [special purpose vehicle] to invest together. In addition, when investing this way, an investor can spread the post-investment responsibilities around and be more helpful and useful to the founder with the focus on scaling and success.

AH: What do you do to help startups become more investment-worthy?

MR: A few years ago, everyone had advice on how to get a pitch and a deck together, including me—I still have a checklist I like—but we weren't focused enough on getting the fundamentals together. It turns out you can teach people how to say just the right things, and put all the right stuff in a deck, but [they] really have no way to actually deliver on it. Now we coach companies to start by thinking through the third meeting with investors. If your deck suggests you can go from $100K in sales this year to $1B in the next three years, the founder better have a really well-thought-out plan of how that's going to happen, what investments are going to be needed, what risks have to be mitigated, whether and how the existing team will be able to execute, when and how new team members will be added, a realistic timeframe for manufacturing, or scaling software, solid customer acquisition costs, etc. We spend 15 weeks hammering on the fundamentals in our fall program for founders. Of the many founders who start our process thinking they are ready for investment, about half realize they've got more work to do. Also, our application process is substantial. Even when a founder doesn't think they will be successful in our process, we encourage them to apply because it creates a set of deadlines, and if they get through entering the things we require, they will have a much better idea of where they fall flat.

AH: Do you see some deficiencies over and over?

MR: Yes. There are six common issues we see:

1. Organizing the deck and pitch as a sales pitch instead of an investor pitch. Sales pitches are about getting you to buy products. Investor pitches are about getting you to buy into the company, team, etc.
2. Misunderstanding of total available market (TAM), serviceable available market (SAM) and serviceable obtainable market (SOM). Defining the market properly tells investors a lot about how the founder will tackle sales.
3. An unclear go-to-market strategy. The times I've seen a founder wreck their own deal by saying some version of "if we only get 1 percent of the market" is too many to count and often a phrase that investors will use to walk away.
4. An unclear timeline or one that shows unrealistic milestones or sales. Numbers and milestones can be crazy, but they need to be supported by clear plans.
5. Failure to make an ask—I've seen half a dozen pitches like this in the last week. Without a specific ask and a clear use of funds that help an investor understand how the founder plans to use the money for scaling—almost always a sales strategy—or specific risk mitigation, founders make it hard for investors to go forward.
6. Simple agreements for future equity (SAFEs). I know they are gaining in popularity everywhere, and they are getting better in terms of protections and upside for investors, but I still detest them. I'd much rather see a convertible note with really clean and standard terms. SAFEs are great for an investor who's looking to make a ton of small investments with the purpose of reserving a spot in the next round, but most of the investors I work with aren't making 50 or 100 investments a year, which is when a traditional SAFE is a good option.

AH: You've got a strong background in economic development. How does that perspective influence your work with angel investors?

MR: At a global scale, we are not going to work our way out of the problems we're facing. Record population, environmental pressure and dozens of other issues will not be resolved by working harder. If we want to feed, clothe and house 8 billion people, and address health, pollution, waste, education and a host of other related problems, we are going to need to invent our way out. Not incremental inventions, but revolutionary and disruptive innovations. Every day we work with companies and angel investors who are making real strides toward solving some of the world's greatest challenges. I am most proud of this work.

At a regional or national level, small businesses are the only businesses that add jobs in the economy. That's an overstatement; but if you look at Fortune 500 companies, they churn employees, and overall employment is flat from decade to decade. Startups add employees, contribute to the tax base and make investments in their communities.

At a local or microeconomic scale, a person who leaves his or her job to pursue something they love and turn their passion into new solutions and meaningful and financially rewarding work changes things first for a family. Successful entrepreneurs can create a living wage, put a roof over their heads, food on the table, take a family vacation occasionally and send their kids to college or help fund the startup of their progeny. Startups create jobs, small businesses get involved in local issues and give to local causes. All of this makes a difference in economic impact.

AH: Music to our ears. Are there any new or interesting trends in angel investing that you're watching?

MR: Since the start of the pandemic, we're seeing more money come off the sidelines—both from new investors and from existing investors who are investing more money. Investors are asking for companies to plan for, and ask for, longer runways. As a result, we're seeing bigger rounds for early-stage companies—two years ago it was $500K; today it's $1–2 million. For our conference this year, we have more companies applying in biotech, healthcare and life sciences. I haven't heard a word for that yet, but we're not the only ones seeing an increase in this space.

AH: We've seen that in Connecticut, too. Here's something I'm really curious about: What's the biggest mistake first-time angel investors typically make?

MR: The biggest mistake first-time angel investors make is putting too much money in their first deal. I've heard the same story over and again: "I didn't know what I was doing, I invested $200K in the first deal. The company went belly up."

AH: Yikes. Good to know. What's your best piece of advice for first-time angel investors?

MR: Join a member-managed fund that has a small unit cost and lets you learn while you build a portfolio. San Diego Angel Conference (SDAC) is one example. TCA San Diego's ACE Fund is another.

Also, get to know some people. There are angel networks and funds all over the place these days. The Angel Capital Association keeps a list. Their resources and networks were amazing when I was first starting out, and they have only become more valuable with time. I'd be remiss if I didn't mention University of San Diego Knauss School of Business: My employer and the home of the SDAC offers both virtual and live workshops on an ongoing basis.

Finally, listen in on podcasts and read some books. Here are my current favorite books:

Angel: How to Invest in Technology Startups—Timeless Advice from an Angel Investor Who Turned $100,000 into $100,000,000 by Jason Calacanis

Angel Investing: The Gust Guide to Making Money and Having Fun Investing in Startups by David S. Rose

Venture Deals: Be Smarter Than Your Lawyer and Venture Capitalist by Brad Feld and Jason Mendelson

The Fundable Startup: How Disruptive Companies Attract Capital by Fred Haney

Secrets of Sand Hill Road: Venture Capital and How to Get It by Scott Kupor

Changing Tides: Powerful Strategies for Female Founders by Jennifer S. LeBlanc

Impact with Wings: Stories to Inspire and Mobilize Women Angel Investors and Entrepreneurs by Suzanne Andrews

AH: I've added all of them to my Amazon cart. Thank you! Last question: Can anyone tune in to your conference in March? Will there be a livestream?

MR: Yes! We're excited to be the only ones who can already say this is our third virtual conference. If you're a student, you can join for free. If you are a professor or teacher, we'd love to host your class and offer some additional special amenities. Find more information at www.thesdangels.com/attend.

AH: Thanks for your time, Mysty! Best of luck with your conference.

MR: My pleasure.