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Crowdfunding and Entrepreneurship

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Synonyms

Contractor; Crowd; Financing; Manager; Microfinancing

Introduction

Crowdfunding is an umbrella term that refers to an ever-growing microfinancing system which, despite not being new, and since cases are already known in the history of the USA where the base of the Statue of Liberty was financed in 1884 by Joseph Pulitzer through calling the US population, which was financed through microdonations (Pitts 2010), has evolved thanks to the Internet and web 2.0 technology, by facilitating access to the "crowd" and by enabling communication and the creation of networks between entrepreneurs and investors (Lambert and Schwienbacher 2010).

Its objective is to promote funds being obtained from numerous individuals who unite their personal contributions to support a specific objective, which might be cooperative, business, prototypes, etc., by, in turn, obtaining not necessarily money-type rewards, but rewards ranging from personalized acknowledgements on the website of the project's creator to preordering products or services at a much lower price before they are launched on the market or even job opportunities (Belleflamme et al. 2014, 2015).

The literature classifies crowdfunding platforms (Giudici et al. 2012) according to: (1) the rights of crowdfunders to participate in a project's outcome; (2) the rates requested by crowdfunding platforms from entrepreneurs/start-ups; (3) the services offered by crowdfunding platforms. The most widely accepted criterion of the rights of crowdfunders to participate allows us to classify crowdfunding projects as follows:

1. Equity-based: crowdfunders have the right to share a part (depending on their level of participation) of the profits that the project makes.
2. Lending-based: funds are returned and crowdfunders have the right to be paid interests agreed on in a contract.
3. Donation-based: funds are provided with no reward involved (for certain philanthropic or sponsored projects).
4. Reward-based: funds are provided in exchange for moneyless rewards (e.g., being cited; obtaining a product version, etc.).

Despite their growing popularity, their academic understanding has centered only on defining and distinguishing the crowdfunding of

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different phenomena, such as crowdsourcing (Afuah and Tucci 2012), online charity donations, and peer-to-peer loans (Zhang and Liu 2012), rather than on analyzing and comparing the advantages and disadvantages of resorting to each model and analyzing it compared to other forms of financing.

In order to analyze and distinguish crowdfunding from other financing alternatives, Hagiu and Wright (2012) facilitated this work for us by providing a qualification of the crowdfunding concept as a "multisided platform": "an organisation that creates value mainly by allowing direct interactions between two different types of affiliated users/customers, or more". On the basis of this definition, it is a platform with many sides or faces on which the main value lies, and one that provides financing, where we find considerable differences with other "traditional" sources of financing:

We assume that crowdfunding platforms are clearly multisided platforms as they are promoted by an organization that will allow direct financing to business projects through numerous individuals via the affiliation (and making contacts) of crowdfunders and the project's entrepreneurs.

As we can see in Table 1, private capital and venture capital, along with business angels, provide business projects with direct financial support but do not have an organization that allows entrepreneurs and investors to be connected. In such cases, business plans are sent directly to the personnel in charge of assessing them and are not publicly available. In these cases, a commonplace practice is investors being affiliated with networks and associations (e.g., European Association of Venture Capital), but the main objective is to place pressure (negotiate) on regulators and banks and to offer services and counselling to subscribers. Some exceptions among business angels can be found, who tend to group in informal networks to share the risk and to co-invest in certain actions.

Stock exchanges are extremely effective financing organizations, and access to them is conceived only through authorized brokers. Quoted businesses contemplate certain specific and formal requirements, but no direct interaction is permitted as operations are centralized and anonymous.

Bank loans are directly given to businesspeople without resorting to the organizations that finance them. The only exception is the platforms that compare the conditions and interest rates among different banks, and which offer brokerage services to companies and consumers, but are generally limited to mortgages and consumer credits.

We also find credit financing companies (leasing, factoring, renting, etc.) through financing organizations that are not affiliated but operate on a resales basis. Furthermore, leasing and credit products tend to be standard, and no direct interaction exists between the company and the end funder.

A Compared Selection of Financing Methods for Business Projects

Many variables have to be taken into account when entrepreneurs wish to decide about the structure of their business capital. The academic literature has centered basically on the business exchange matters between debt and financing of capital (e.g., Chua et al. 2011; Zhang 2014). For instance, the studies by Chemmanur and Fulghieri (2014) and by De Bettignies and Brander (2007) identify many surprising differences between debt and financing of capital, such as: (1) banks' financing provides strong incentives for entrepreneurs, which leave businessperson complete company ownership, while financing of capital dilutes the businessperson's incentives to provide the required effort; (2) banks are relatively passive investors, while venture capital suppliers normally provide businesspeople with management firms; (3) financing of capital tends to take longer to accumulate than financing debt; (4) direct bank loans must reach a given volume to finance projects and to cover administrative costs, whereas financing of capital tends to be more flexible (e.g., business angels).

Therefore, in the literature we can see that rewards exist in certain aspects like control and ownership, which depend on the types of financing that entrepreneurs follow. After reviewing the literature on the advantages and disadvantages of

Crowdfunding and Entrepreneurship, Table 1 Comparison between crowdfunding and other sources of finance for small venture projects

	Crowdfunding	Venture capital and private equity funds	Business angels	Stock exchanges and trading platforms	Bank loans	Leasing finance/trade credit
Enabler organisation	Yes	No	No	Yes	No	Yes (w.e.)
Direct interaction	Yes	Yes	Yes	No	Yes (w.e.)	No (w.e.)
Affiliation of investor/ investee	Yes	No	No (w.e.)	Yes	No	No

(w.e.) = with exceptions

different sources of capital for business companies, we found (Table 2):

Understanding the Functional Nature of Crowdfunding Platforms

We distinguish at least two crowdfunding platform parties: funders and fundraisers. A funder establishes a relationship with a fundraiser by promising a certain amount of money to a particular project.

Crowdfunding platforms display positive crossed external effects between donors and fundraisers. Let us examine the two types of external effects:

1. External effects on funders/donors: they tend to prefer platforms with a larger number of campaigns and, therefore, with a larger number of fundraisers as this enhances their capacity to select which project to finance.

   Yet there may be cases in which funders are more attracted by a platform with a smaller number of campaigns as this increases the probability of any given campaign achieving the financing requirements that they need (a higher concentration of funders per project). Thus they depend on the balance between "the variety and chance of co-financing" so that positive effects on fundraising groups exist.
2. External effects through crowdfunding platforms' functioning: quite often effects also exist "within" crowdfunding platforms, and these can be positive or negative: it is likely difficult for a fundraiser, for any given number of funders, to obtain the necessary funds for his/her project if more competitive campaigns exist. Conversely, a funder may prefer to be alongside a larger number of followers because, for example in this case, funders would not be competing, but would simply benefit from a higher probability that the project is undertaken. However, if a project has a set size, funders might perceive its funding companions as being competitors as they might lose an interesting project.

Prices Structures

When it comes to evaluating the cost of the crowdfunding platform itself, we must consider the platform's costs for entrepreneurial projects as crowdfunding platforms generally have three sources of income:

One: they earn interests on the money spent on a given campaign as funders transfer money at the time they contribute. This money is transferred to fundraisers if the campaign is successful, or it is returned to funders if it is not. In the meantime, the platform can earn interests on these funds. So donors make lost interest when they (temporarily) invest in a project.

Two: some platforms offer additional services which they charge for. In particular, many charge to manage payments. They may also offer services that come from third parties and obtain income from third suppliers; e.g., the income from the French platform Spear is based on offering additional services to support the project (1% of the amount loaned), as well as 3% from subscription

Crowdfunding and Entrepreneurship, Table 2 Sources of entrepreneurial finance (Source: Wu et al. 2016)

Sources of entrepreneurial finance	Specific types	Advantages	Disadvantages	Sources
Formal equity	Venture capitalists	1. Provide monitoring services; 2. Provide a variety of support services; 3. Certification	1. Surrender partial ownership of the venture; 2. Dilute the entrepreneur's incentive to provide effort	De Bettignies and Brander (2007); Denis (2004)
	Angel investors	1. Plays an important networking role; 2. Shorter time until venture financing; 3. The unique role in fund equity	1. Relatively small equity stage provides few postinvestment support services; 2. Lacks a clearly stated mission; 3. Inherent conflicts of interests between the corporation and entrepreneurial venture – little incentive to provide value-added support service	Chemmanur and Fulghieri (2014); Denis (2004)
	Corporate venturing	1. Have longer investment horizons than traditional VC firms	1. Lacks a clearly stated mission; 2. Lacks sufficient commitment; c. conflicts over the strategic direction of the start-up	Chemmanur and Fulghieri (2014); Denis (2004)
Informal equity	Informal crowdfunding	1. Raises funds from a large number of investors	1. Increases the chance that investors will lose money; 2. Crowdfunding may not be beneficial for the long-term success of entrepreneurial firms	Chemmanur and Fulghieri (2014)
Formal debt	Bank loans	1. Leaves entrepreneur with full ownership to avoid diluting entrepreneurial effort and loss of entrepreneur control	1. Deprives the firm of VC's managerial input; 2. Needs collateral that is acceptable to banks; 3. The amount of the loan needs to reach a certain scale	Talavera et al. (2012); De Bettignies and Brander (2007); Zhang (2014)
Informal debt	Debts from friends, family, money lenders	1. Detailed personal knowledge of the client is available	1. Costs and interest rates can be affected by the relationship between the lender and the borrower; 2. Loans are small and short-term to reduce default risk; 3. The nominal rate is sometimes higher than that of formal sector loans, especially in rural areas; 4. Incurs reciprocal financial obligations	Chua et al. (2011); Zhang (2014)

rates. Other possible services could include disseminating information about former projects; some diagnostics can be valuable for donors and others for fundraisers, etc.

Three: many platforms charge a transaction fee. This fee might be conditioned to a campaign being successful. As documented in Massolution (2013), most platforms charge fundraisers a transaction fee on a percentage basis for all successful campaigns; do not charge for unsuccessful campaigns (the French platform Octopusse charges a

7% financing fee if the campaign is eventually successful).

Other alternatives exist; for instance, charging fees to become a member or to subscribe for a given period.

Some of the Most Relevant Crowdfunding Platforms for Entrepreneurs

As the "lifeline" of SMEs and future entrepreneurs, crowdfunding platforms are a way to gain credit for ideas and projects by encouraging the participation and interaction of various actors in the professional and business environment. When the World Bank announced that crowdfunding would have a value of up to $90 billion between 2020 and 2025 and Forbes announced that crowdfunding would be valued at $90 billion by 2017, which surpasses the Venture Capital trend all together, the world (investors, start-ups, and regulators alike) realized that it was time to join the trend.

The types of interaction that one can experience between the participants in these platforms vary immensely and allow start-ups and investors to find which solutions best fit their needs and desires.

Kickstarter: is perhaps the most well-known one with a history of launching successful products, like Pebble Watch, the games console Ouya (which exceeded 8.5 million US dollars in 1 month), independent films, music, among many others. In 2014, its fundraising exceeded one billion dollars with more than 5.7 million people. Those who seek financing set an objective and then have a limited time to raise the required money before their project expires. This platform, in turn, ensures the creation of a community around a project to help launch it and to have a broader scope (a platform centered on the USA, Canada, the UK, Australia, and New Zealand). What is good about the Kickstarter system is that it is the "all-or-nothing" kind: i.e., the funder's credit card will not receive payment until the project meets its objective.

Indiegogo: it works like Kickstarter, but its distinguishing aspect is that it is not limited to an "all-or-nothing" strategy because it also allows what is known as "flexible" financing: it pays your money to the entrepreneur, even though you have not been able to reach the requested total. However, the financed party should pay its rewards. The site states that this works better for projects that do not require much help and for those that need to focus not only on real physical products, but also on social and creative initiatives. The Indiegogo and retailers association provides high-added value as the site has reached agreements with companies like Amazon and Brookstone to help them to manufacture and take products to the market. Some past examples of successful projects include the Jibo Family Robot, the Solar Roadways Project, and the effort made to teach children how to code.

GoFundMe: for those entrepreneurial projects which seek to finance projects that fall outside the spectrum of gadgets, GoFundMe has become a popular alternative that allows it to raise funds for social change and its dissemination/promotion. Some of its projects have used the site to raise funds for families who have lost loved ones or personal belongings owing to catastrophes or tragedies, to support efforts to help in disaster situations, and for medical research, and even to establish a central place where sympathizers provide help to partners after they decide on a formal compromise.

YouCaring: to go even further to help people affected by personal tragedy, YouCaring has become one of the most important platforms that supports families, afflicted persons, and people with difficulties. YouCaring allows users to set objectives, but operates in a "help" system. Anyone can configure a YouCaring page, and the site offers a useful characteristic that allows daily access to funds, which is particularly important for medical invoices and expenses that need paying daily or require formulations.

Crowd Supply: it is less known than the previous platform. It consists in a launchpad for new open hardware projects, hackables, and high-range products for freaks. It allows creators of products to put their ideas into practice. It is the only platform of this kind that has been backed by the Free Software Foundation for respecting its users' privacy and freedom, and it is the only crowdfunding platform where each financed product has materialized and been delivered to sponsors. Some of its notable product launchings include the Novena open hardware laptop by bunnie & xobs, the Purism Librem laptop, and the peel-and-stick circuit stickers by Jie Qi.

Crowdfunder: is for those who wish to act as a "venture capitalist" instead of simply financing a project. Rather than obtain rewards for different financing levels, it gains a share of the company itself. Unlike other services, it requires a minimum investment, which can become thousands and even dozens of thousands of dollars. So if the project works well, the reward can be significant (or might not be).

Experiment: like Kickstarter, this site uses an "all-or-nothing" financing model. If the project does not meet its financing objectives, no one will suffer or be accused. Another goodwill aspect is that all projects must be preapproved.

Experiment: love for science. Anyone can present their research proposal. However, before it is launched, it will be reviewed to ensure that the underlying research is solid, and the project is feasible. It is also possible to see the whole scientific process route as the people in charge of the research project should make every effort to be transparent to sponsors (a few dozen scientific articles have been published in high-impact journals as a result of campaigns backed by Experiment).

Chuffed: if you are a fan of nonprofit projects, Chuffed is a suitable site for you. It contains no luxury gadgets, only groups that work on a range of social themes that need your help. As with Experiment, anyone can send their project for crowdfunding purposes, but Chuffed has an interesting way of doing this. This site asks for the project pitch to contain 50 words or less, and it will be approved for crowdfunding if it is liked. If after all the project leader can describe what it is doing, or what it wants to do, briefly and concisely, this means (according to those in charge of the site) that there is a better chance of its effort and proposal being taken seriously.

For the specific case of Europe, and thanks to the "Action Plan on Capital Market Unions", we can see how the European Commission has begun to take the necessary measures to explore these financing alternatives "to reinforce Europe's economy and to stimulate investment to create job posts," with an investment plan of 315,000 million euros. At CSW Europe 2015 in October during the European Forum for Entrepreneurial Finance: "it is necessary to equip the masses so they can utilise these platforms, forge strong risk management and finance literacy based on the principles of crowdsourcing."

Moreover, equity crowdfunding platforms in Europe are advancing in all these matters (European Commission 2017). What platforms in Europe are making successful equity crowdfunding campaigns? According to Crowd Sourcing Week, 2015; CrowdExpert.com (Massolution 2015; Crowdfunding Industry Statistics, 2015–2016), we now go on to highlight some of the most relevant ones:

Companisto: The Berlin-based equity crowdfunding allows crowd investors to invest for as little as €5 up to €500,000, with no limit for companies on how much funds they want to raise. Companisto has funded companies and start-ups from various industries, such as real estate (Weissenhaus has raised €7,500,000), food, toys, digital tech, among others. The company has received a more than €24-million investment from 44 K investors and has funded 51 projects.

Crowdcube: is a UK-based equity crowdfunding platform that allows entrepreneurs and SMEs to raise capital in various industries, such as Art & Design, Consumer Electronics, Film & TV, Professional Businesses and Services and, among others, via equity, debt, and investment fund options. On this platform, you can be a private "crowd" investor where you can receive shares from the companies' released shares you have supported. At the time of writing, Crowdcube has successfully funded more than £122 million with 300+ successful projects. Want to raise your first campaign? Companies need to be a UK Ltd. company to get started and, from the investors' side, you can invest in as little as £10.

FundedByMe: is a crowdfunding portal based in Stockholm, Sweden. The company is active in Scandinavia and has offices in Singapore and Malaysia. FundedByMe's native language is English, but users can list their project in any supported language. The company was founded in March 2011 by Arno Smit and Daniel Daboczy. [1] In September 2012, the company launched FundedByMe equity, an equity crowdfunding portal, in addition to its donation crowdfunding portal. The FundedByMe portal operates on the "all-or-nothing" funding principle, where investments are made on a pledge basis, and pledges are not released unless the project meets or exceeds a preset funding target. By February 2012, FundedByMe had reportedly conveyed over USD $1 Million to "mostly smaller projects" to launch businesses, fund equipment purchases, or back project concepts. The FundedByMe project reportedly raised its own launch capital via crowdfunding. The company has listed various cultural projects, and also "includes journalism as one of its categories" that focuses on projects from countries in Africa, Europe, Asia, and the United States.

Invesdor: Invesdor is a Helsinki-based equity crowdfunding platform and was the first to operate and provide alternative financial services in Northern Europe. It has served as a matchmaker between investors and businesses since May 2012. If you want to invest in a diverse group of companies and services, whether in real estate, food chains, or in digital platforms, this is a good platform for Nordic start-ups, entrepreneurs, and crowd investors. Invesdor has raised more than €10 million euros, with 47 successful rounds and 111 listed companies. As an entrepreneur, you can start raising funds from as little as €20,000 and up to €1,500,000 during the open round.

Invesdor focuses on equity crowdfunding for start-ups and growth companies. Finnish, Swedish, Danish, and UK companies can raise up to 2.5 million euros through Invesdor, while investments can come from anywhere in the world. The minimum for each investment is €20. The service follows the "all-or-nothing" model, in which pledged funds are collected only from investors if the minimum goal set by the company being funded is reached by the end of the crowdfunding campaign. The company seeks to position its service as a low-threshold option by having a low minimum investment and a general scarcity of paperwork during the process.

MyMicroInvest: a Belgium-based crowdfunding platform, MyMicroInvest allows you to invest alongside with professional investors in Europe for as little as €100 in start-ups and SMEs. The company has received investments of more than €12 million and has funded 40 companies from their 30 K+ members.

Seedmatch: Known as Germany's crowdfunding platform for start-ups, Seedmatch is also a matchmaker between investors and start-ups and allows investors to get their equity shares starting from €250 for an individual portfolio. On the flipside, start-ups can raise funds as little as €100,000. As of this time, the company has received investments of more than €24 million with 82 funded projects and a 95% success rate.

Seedrs: is an equity crowdfunding platform for investing in start-ups and later-stage businesses throughout Europe. Seedrs allows users to invest as little as £10 or €10 in the businesses they choose and permits early-stage start-ups and more established businesses to raise investment from friends, family, customers, angels, and other independent investors in exchange for equity in the business. The platform offers three types of campaigns for investment: equity, funds, and convertible campaigns.

Seedrs is an "all-or-nothing" platform where companies do not receive any funding unless they reach their declared investment target, but businesses have the chance to accept more than originally asked for in a process called "overfunding". It allows a wider base of potential investors, among the mass affluent, and access to start-up investing, an asset class that was previously only available to high-net-worth or sophisticated angel investors.

Symbid: (aka The Funding Network) is a Netherlands-based equity crowdfunding that provides traditional and new ways of financial alternatives for entrepreneurs. You can invest as little as €20 to jumpstart your investments in promising start-ups. The platform boasts a solid community of 35,515 registered private investors and 51 professional investors and has received over €417 million in investments.

SyndicateRoom: operates according to the "investor-led model" where it has a syndicate of investors around professional investors, while allowing a crowd of online investors to invest in British companies in both their early and late stages. As the name speaks for itself, it builds a syndicate of investors via equity. In a nutshell, you can invest with the "Angels" and have the opportunity to learn how they play around on shares. SyndicateRoom bagged the Alternative Finance Platform of the Year in UK at the 2015 AlFi Awards. Since its founding in 2013, it has raised more than £40 million. You can register as an introducer to leverage the network of investors or as an entrepreneur where you can start with a minimum equity funding of around £150,000. From the investor's side, you can start investing with as little as £1,000.

Ulule: a leading crowdfunding platform in Europe that also works with very high figures and has successfully financed over 16,719 projects. It follows the "all-or-nothing" model; i.e., if you do not achieve the fundraising that you requested for your project, no rewards are requested. Any projects taken on are published in Europe and can vastly vary from sporting to creative ones and even ecological ones.

Wiseed: a France-based equity crowdfunding platform in real estate allows you to invest collectively for as little as €1,000. You can invest in a variety of properties, such as commercial properties, farms, residential properties, etc. Wiseed comes with three options: invest in start-ups (invest for as little as €100), in real estate properties or get funds via cooperatives. At the time of writing, Wiseed has raised a €36-million investment and has funded 89 projects.

Cross-References

▶ Angel Investors
▶ Bank Loans
▶ Contractor
▶ Corporate Venturing
▶ Crowd
▶ Crowdfunding
▶ Debts from Friends, Family, Money Lenders
▶ Entrepreneur
▶ Financing
▶ Manager
▶ Small Venture Projects
▶ Venture Capitalists

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