

Crowdfunding

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Crowdfunding is the practice of funding a newly created firm or project by raising funds from a large number of people. It is usually performed online. In 2009 the volume of funds raised using crowdfunding was negligibly small. Crowdfunding raised \$34.4 billion in 2015. Some analysts predict that crowdfunding market size will grow at an annual rate of 27.8% and will surpass venture capital investments in the near future (Miglo and Miglo, 2019).

Keywords: crowdfunding ; reward-based crowdfunding ; equity-based crowdfunding ; debt-based crowdfunding ; donation-based crowdfunding ; "all-or-nothing" (AON) ; "keep-it-all" (KIA)

1. Definition and Overview

Crowdfunding is a form of fundraising whereby groups of people pool money, typically (very) small individual contributions, to support a particular goal (see eg. Ahlers, Cumming, Guenther and Schweizer (2015)^[1]). It is usually performed online. There are different types of crowdfunding. Under reward-based crowdfunding, investors count on some extra-benefits from the company such as future product discounts. Under equity-based crowdfunding investors will receive shares of the company. Under debt-based crowdfunding, (also known as "peer to peer" or "P2P"), investors make loans to individual borrowers or bundles of borrowers. Under donation-based crowdfunding, funds are raised for social purposes. Reward-based crowdfunding campaigns are commonly offered in one of two models. The "Keep-It-All" (KIA) model involves the entrepreneurial firm setting a fundraising goal and keeping the entire amount raised, regardless of whether or not they meet their goal, thereby allocating the risk to the crowd when an underfunded project goes ahead. The "All-Or-Nothing" (AON) model involves the entrepreneurial firm setting a fundraising goal and keeping nothing unless the goal is achieved, thereby shifting the risk to the entrepreneur (Miglo and Miglo (2019)^[2]).

2. Existing Literature

Crowdfunding research is quickly growing. Moritz and Block (2014)^[3], Cumming and Hornuf (2018)^[4], Estrin, Gozman and Khavul (2018)^[5], Mochkabadi and Volkmann (2018)^[6] and Cumming, Leboeuf and Schwienbacher (2019)^[7] provide good reviews of the literature in this field.

Some examples of empirical research include Agrawal, Catalini and Goldfarb (2010)^[8], Ahlers, Cumming, Guenther and Schweizer (2015)^[1], Hildebrand, Puri, and Rocholl (2014)^[9] and Mollick (2014)^[10]. These papers manifested an immense level of interest for crowdfunding among practitioners. These papers found the following: crowdfunding relaxes geographic constraints on fundraising, which inhibit venture capital and angel financing; asymmetric information and signalling play a significant role in crowdfunding; the success of a project and any potential delays are related to the volume of financing it receives; the timing of contributions usually follows a pattern etc.

Among theoretical papers note the following. Miglo and Miglo (2019)^[2] consider the role of different market imperfections in explaining the choice between reward-based crowdfunding and equity-based crowdfunding. For example, they find that under asymmetric information high-quality firms prefer reward-based crowdfunding and use it as a signal of quality. Strausz (2017)^[11] argues that under demand uncertainty, crowdfunding improves screening for new projects. Entrepreneurial moral hazard threatens this advantage. Crowdfunding enable consumers to implement staged payments and thereby manage moral hazard. Schwienbacher (2018)^[12] analyzes risks related to crowdfunding campaigns. Reward-based crowdfunding offers a signal about the overall market potential of the entrepreneur's product. Raising money from professional investors does not offer the same informational feedback, since their decisions are mostly based on the assessment of the overall profitability of the investment opportunity and not on consumption. Miglo (2020a)^[13] studies the role of crowdfunding in a competitive environment. The opportunity to observe both the funders' demand and the strategies of their competitors during the pre-sale stage helps firms improve their spot sale pricing and production decisions even if the pre-sale stage is costly (firms pay rewards to funders participating in the pre-sale stage). Miglo (2020b)^[14] considers a model of the choice between the different types of crowdfunding, which contains elements of the

asymmetric information approach and behavioral finance (overconfident entrepreneurs). Belleflamme et al (2014)^[15] argue that the value of equity-based crowdfunding can be higher under asymmetric information than under symmetric information.

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