



What if crowdfunding becomes the leading source of finance for budding entrepreneurs or growing companies?

Can crowdfunding offer a viable source of funding to growth orientated businesses around the world? 2015 promises to be a big year for crowdfunding in terms of the role it may play in getting entrepreneurial ventures off the ground. What might that world look like if it became the leading source of finance for companies starting out? To that end, one has to better understand the phenomenon and its rapid expansion to date.

Why now? In 2014, the total global capital raised through crowdfunding platforms stood at \$16.2bn, according to a study by crowdfunding research firm Massolution which was cited by the Economist. The number of crowdfunding platforms has experienced dramatic growth over the past decade. In Europe alone, I've observed the number of platforms growing from less than a dozen in 2009 to more than 10 times that in four years. Policymakers, to a large extent, have catapulted crowdfunding into global awareness.

The Jumpstart Our Business Startups ACT in the US, and similar legislation across the world, opened the 'regulatory door' to this innovative funding approach. Before the act was passed in spring 2012, crowdfunding sites could reward investors with just products or discounts. But the act has given them the freedom to offer backers a stake in the business.

By analogy, the origin of the venture capital industry is often credited to another regulatory change, the Prudent Man Rule of 1979, which allowed US pension funds to allocate a fraction of their assets under management towards risky investments. A supportive regulatory environment will be instrumental to the continued growth of crowdfunding as a credible and persistent alternative. It follows that crowdfunding will proliferate in those countries where regulators can balance the potential – and challenges – associated with the funding source.

Of the different types of crowdfunding models, there are four in particular experiencing high levels of traction:

- Donation-based (where contributors are motivated by social or intrinsic goals)
- Rewards-based (where contributors are effectively pre-purchasing a product or service)
- Debt crowdfunding (where contributors receive a debenture)
- Equity crowdfunding (where contributors receive an equity stake in the funded company).



Success and failure can look very different for venture capitalists and crowdfunding investors. Oculus Rift, the virtual reality headset developer, is a case in point.¹ In 2012, the company secured \$2.5m from more than 10,000 individuals on the reward-based platform Kickstarter. Yet, the \$2bn Facebook acquisition two years later did not generate the anticipated jubilation among the crowd who'd supported the deal from the start. Rather, the media reflected contributors' disappointment and anger, such as "*I Backed Oculus Rift On Kickstarter And All I Got Was This Lousy T-Shirt*".²

The discussion charts the nature and scope of crowdfunding's ultimate success. New pools of capital will become available alongside traditional investors (i.e., angels, VCs, or banks) as well as in previously underfunded domains (e.g., deployment of renewable energy solution, or social housing).

¹ <http://www.theguardian.com/commentisfree/2014/mar/27/oculus-rift-facebook-buy-out-kickstarter>

¹ http://www.huffingtonpost.com/2014/03/26/oculus-rift-kickstarter_n_5034511.html

The key to realising such potential is threefold. First, it calls for informed entrepreneurs and contributors. Of course, financial reward is a marker of success. But it's also important for entrepreneurs to recognise the value of fostering strong relations with their contributors, keeping their own ambitions and their contributors' reasons for supporting them aligned. Second, the funding landscape will need to adapt to specific demands. Different crowdfunding solutions will suit different start-up phases, for example working capital needs may be financed through pre-order sales on reward-platforms, while specific objectives such as meeting upfront fixed costs might be done via contributions on donation-platforms. Third, it will need a robust regulatory framework to support its development and growth. The right regulatory oversight will reflect the realigned landscape and offer a prudent environment that ensures transparency and safeguards to the crowd of investors.

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