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**CROWD – FUNDING: DEVELOPING A STRATEGY
FOR CROWD PARTICIPATION**

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Abstract

Crowd-funding is a new fundraising method that utilizes the power of the Crowd. Even though it has attracted the interest of academics and professionals, there is a lack of in-depth research on the crowd-funding method. This paper aims to create a participation model, and it sets a marketing framework based on the extant literature from different disciplines that they are related to crowd participation. Different motivators that lead to the participation in a crowdfunding campaign have been found in the literature, yet according to different studies social motives have the strongest influence among others on the participation. Also this paper proposes Entrepreneurial Marketing as a new thought in the marketing discipline; Entrepreneurial Marketing not only helps entrepreneurs to meet their specific strategy goals, but it also provides a framework that leads to a better understanding of the method itself.

JEL: G21, G24, M31, Z1.

Keywords: Crowd-funding, Crowd-sourcing, Social Media, Entrepreneurship, Entrepreneurial Marketing, Finance method.

CROWD – FUNDING: DEVELOPING A STRATEGY FOR CROWD PARTICIPATION

Introduction

The first time the Crowd-Funding method has been mentioned in the international literature was in 2006 by Jeff Howe. According to Jeff Howe the Crowd-funding method consists one of the four Crowd-sourcing strategies; the other three strategies of Crowd-sourcing are Crowd creation, Crowd voting and Crowd wisdom. The Crowd-sourcing method involves outsourcing tasks to a distributed group of people. This process occurs mainly on-line, through Web 2.0 technologies (Braham, 2008; Howe, 2006), and offline. The outsourcing tasks that are utilized by Crowd-sourcing could be for instance, the improvement of a product or service, the promotion of a product or the funding of a new venture. It is important the Crowd-sourcing method to be highlighted in order the Crowd-funding method to be accurately understood; the factors that influence and defines Crowd-sourcing influence crowd-funding as well. This will set the background for explaining the different motives of the players that interact within the crowd-funding system.

The crowd-funding method aims to fund new ventures, which have been proposed, through the collection of small and medium investments from the Crowd (Ordanini, 2009). This definition demonstrates the different parts that take part in crowd-funding: the person or group of people that propose the task, the crowd-funding platform in the internet, and the crowd or the co-investors that invest their money in the project. The web based platform is used to collect money and also to guarantee the smooth interaction of the different parts that they interact in the crowd-funding system

During the last decade Venture Capitals fail completely to make profits by investing in new entrepreneurial ventures, as the 75% of the total investment makes no profit at all. For that reason, Venture Capitals are in pursuit of the next economic “bubble” to invest in (Gibney and Howery, 2012). The crowd-funding method has a quite clear goal; to collect money from the crowd in order to fund new ventures that could also be an entrepreneurial one; a goal that comes to fill the gap that was created by the reluctance of Venture Capitals to invest in new projects. Moreover Lam (2010) has noted that entrepreneurs have to find new and more innovative sources of capital than those categorized as formal sources of capital due to the reluctance of the later to fund them. There is a need of capital in the market and Crowd-funding could be an alternative source.

As an innovative and entrepreneurial method of funding, the most appropriate marketing philosophy that could provide an orientation for the method in the market is that of the entrepreneurial marketing. Marketing according to the American Marketing Association is "the creating, communicating, delivering and exchanging of offerings that have value for the costumers, clients, partners and society at large." Obviously Crowd-funding has a great dependence of the marketing discipline in order to achieve its goal. Entrepreneurial Marketing literally is the interface of marketing and entrepreneurship, and it attempts to be somewhat more specific for new businesses. Entrepreneurial Marketing provides the conceptual and theoretical tools in order to comprehend the implementation of entrepreneurship. Such a theoretical tool is for example the 4P's (Person, Process, Purpose, Practice) proposed by Zontanos and Anderson (2004), which gives a new perspective to the implementation of entrepreneurship through Crowd-funding also.

Crowd-funding is an interesting research area, however, as a new method it is not very well-established. Therefore, additional literature on relevant analogies of participation has been examined in order to analyze and ask the research questions have been set in this paper. What's more, literature in psychology and sociology is being reviews along with marketing and financial concepts and theories. Apart from the development of a crowd-funding participation model this paper seeks to answer the following research questions:

- Could crowd-funding method be incorporated to all entrepreneurial ventures?
- Are there any benefits for the production of commodities and the delivering of services and if so, for what kind of products and services?
- Does the classic Marketing concept benefit a crowdfunding strategy?

Literature review

The investment gap

Both national and international entrepreneurship is regarded as a catalyst to economy (Kirchhoff, 1991; Benneworth, 2004; Grilo and Irigoyen, 2006). The importance of this factor has attracted the interest of many researchers in the domain of entrepreneurial finance. (Fletcher, 1995; Harris, 1995; Cowling and Westhead, 1996; Hamilton and Fox, 1998; Carter et al, 2007, Franke et al, 2008).

A new entrepreneurial venture can be financed from formal or informal sources of funds. A source can be categorized as formal or informal according

to certain criteria such as, visibility, the resources they own and the way they are organized (Lam, 2010). Thus, for example Venture Capitals are considered formal source (Butler and Ulin, 1950; Shepherd and Zacharakis, 2002; Busenitz et al. 2004; Florin, 2005; De Clercq and Sapienza, 2006; Pintaro et al., 2007; Franke et al., 2008; Li, 2008) and Business Angel an informal source (Mason and Harrison, 1996; Harisson et al., 1997; Steir and Greenwood, 1999, Sorheim and Landstrom, 2001; Mason and Harrison, 2002; Robinson and Cottrell, 2007).

More than ninety per cent of new ventures are financed by informal sources of finance, while sixty percent of start-up capital is finance by the business founders (GEM, 2004). The problem became more evident in a Global Entrepreneurship Monitor (GEM) report in 2003 (p.31) where it is reported that *“Venture capital is so rare, that maximum a hundred or so companies have venture capital in hand at their birth, in contrast to millions that have been financed by informal investments.”* Also, a UK national scale survey for small businesses found that those ventures which had used equity finance tended to be larger businesses operating for around four to ten years and which had a number of employees (SBS, 2004). Moreover, a survey that was conducted in the European Union Countries about their attractiveness for investments, shows that the criteria are set by Venture Capitals cannot be found in many of them (Groh, Liechtenstein and Lieser, 2010). The findings of these studies underline that there is a “gap” in the great demand for finance on the one side, and a limited supply on the other, the so called “investment gap”.

The informal source of finance has been proven to be the most promising way to fill the “investment gap”. Except for studies on business angels there is a number of studies on informal sources as entrepreneur’s families and networks (Chotigeat et al, 1990; Bates, 1997; Basu and Parker, 2001). Families and friends regarded as the first sources of capital, here it is worthwhile to be mentioned that crowd-funding can utilize those informal capital sources and also to incorporate them with a larger network of people that can be found both on-line and off-line.

Crowdfunding History

Crowd-funding is not a new concept; it has actually been being used for centuries since society utilizes networks in order to fundraise money from charities and donations so to build schools and social facilities. There are written evidence in Hanifan’s (1916¹) studies about the local support for rural schools. Also even the case of the statue of Liberty is such an example, except for being a symbol of democracy, it is the work of charity from both French people

¹ http://en.wikipedia.org/wiki/social_capital

that donated money to build the statue and the Americans who donated to build the pedestal. Crowd-funding is just the Darwinism of donation; the factors that lead to the genesis of the method are both technological and sociological. Those factors especially are: the evolution in computing and web 2.0 makes the interaction of people from all over the world easier as never before in human history (Jones, 2010), the advent of social media has changed the way people network and finally a boost to Crowd-funding method has been given by the improvement of payment methods, while it is much easier and safe to transfer money all over the world. Society defined as the aggregation of different groups of people, on the other hand, has started to play a central role in business practice; outsourcing methods that business utilizes is an evidence that society is considering to be “a problem solver”. This swift has been reported from sociologists (Brabham, 2008; Lennart, 2009) and also scientists from different disciplines like the Surowiesky (2004) and Sunstein (2006) that enthusiastically express the aforementioned notion with the phrase that “the crowd is wise”.



Picture 1: factors that evolve crowd-funding method

In the mid-90's internet communication between people started to go beyond email exchanges by the launch of AOL Messenger² and the SixDegrees.com³. That heralded the advent of a new era in the way people interact with each other and at the same time expressed the need for a further development of computing technologies and applications. At the late 90's some internet campaigns that aimed to collect funds appeared⁴. In 2005 Kiva⁵, the first platform that allows entrepreneurs from developing countries to borrow money was launched. The establishment of Kiva was substantial to the evolution of crowdfunding and although a controversial project, Kiva is still a successful platform. It has already raised \$295 million, with an outstanding of 98,94% repayment rate. Kiva's successful model for lending money was developed and expanded into what is now known as peer-to-peer⁶ lending or person-to-

² http://en.wikipedia.org/wiki/AOL_Instant_Messenger

³ <http://www.sixdegrees.com>

⁴ http://en.wikipedia.org/wiki/Marillion#Brave.2C_Afraid_of_Sunlight_and_split_with_EMI_.281992.E2.80.931995.29

⁵ <http://www.kiva.org/about>

⁶ http://en.wikipedia.org/wiki/Peer-to-peer_lending

person lending which occur between “peers” without the intermediation of traditional financial institutions. The first site that adopts the new “peer-to-peer lending “model was Zopa⁷, followed by Prosper⁸ in 2006 and LendingClub⁹ in 2007. Those platforms were not particularly successful in the beginning because of overly tight regulations and maybe because society was not quite ready for such changes at that point.

In 2008-2009 innovations such as Facebook¹⁰ and Open ID¹¹ changed completely the way people interact and communicate. Every experience from then and on can be shared in Social Media platforms with people from all over the world, people can interact using those platforms without any geographical limitation. This change has helped people to expand their social networks. In the period 2008-2009 IndieGoGo¹² and Kickstarter¹³ was launched and both became very popular at that time, so popular that after 2 years Kickstarter set the world record for the largest amount of money that have ever been raised using crowd-funding for the Tik Tok + Luna Tik ¹⁴ project. Between November and December of 2010, 13512 people “pledged” \$942.578 for the Tik Tok +Luna Tik project. After the success of Kickstarter and IndieGoGo, a plethora of new reward –based crowdfunding platforms appear every day, many of them are niche-targeted or limited to a specific geographical area or a specific community, or differentiated in some way. Therefore, crowd-funding as a method was established literally by the advent and mass acceptance of Kickstarter and IndieGoGo. Crowdfunding since then has continued evolving and in 2010 the first equity-based Crowdfunding was founded by GrowVC¹⁵ while in 2011 it was followed by Crowdcube¹⁶ and in 2012 by the Greek StartersFund¹⁷.

⁷ <http://uk.zopa.com/>

⁸ <http://www.prosper.com/>

⁹ <http://www.lendingclub.com/>

¹⁰ <http://www.facebook.com/>

¹¹ <http://openid.net/>

¹² <http://www.indiegogo.com/>

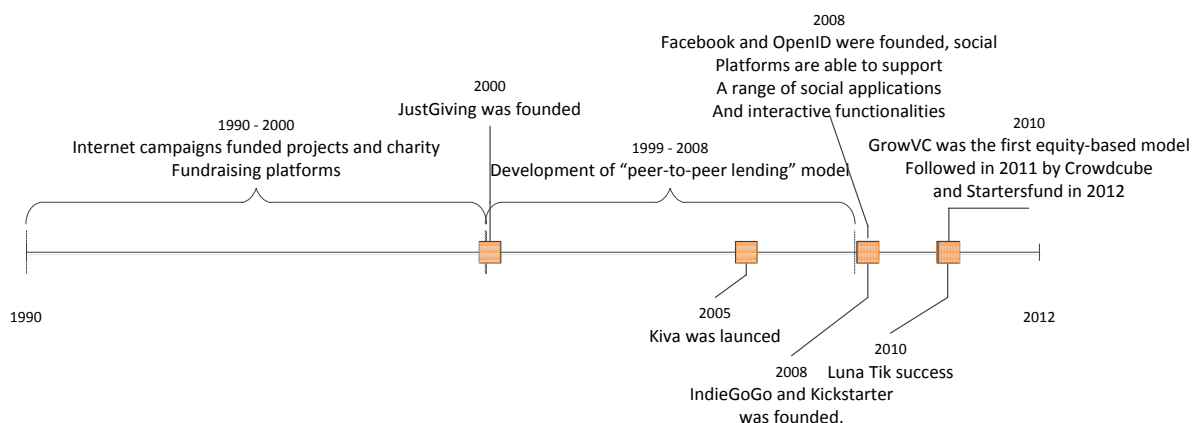
¹³ <http://www.kickstarter.com/>

¹⁴ <http://lunatik.com/>

¹⁵ <http://www.growvc.com/main/>

¹⁶ <http://www.Crowdcube.com>

¹⁷ <http://www.StartersFund.com>



Picture 2: Crowd-funding evolvement

Different motivations for people to contribute to projects through crowdfunding platforms.

Crowd-funding is a new method; regardless of being a topic of interest from both the academic community and entrepreneurs, it has not been very well established yet. In order to examine the different motives and incentives that lead people to contribute to projects through crowd-funding, this paper takes into account studies from different sciences with the same analogies in participation along with studies from psychological and sociological disciplines. The main topic of the examined literature is crowdsourcing, as crowd-funding is a strategy of crowdsourcing the mechanism of the participation is the same.

Methodologies that have been adopted by different authors vary from quantitative (Chinman, Anderson, Imm, Wandersman & Goodman, 1999; Huberman, Romero & Wu, 2008) to qualitative and experimental (Brabham, 2008; Chanal & Caron-Fasan, 2008; Harris, 2010; Holley, 2010; Horton & Chilton, 2010; Leimeister, Huber, Bretschneider & Krcmar, 2009; Mason & Watts, 2010; Poetz & Schreiner, 2012; Schenk & Quittard, 2011; Van Sylke & Brooks, 2005).

Poetz and Schreier (2012) stress that the industry and the product category are of great importance to the contribution people can make and also for the outcome of the activity. Along with the findings about the industry and the product category, different studies have noted also that if the knowledge base- entry barriers are high people will be discouraged to participate (Baldwin et al., 2006; Lettl, Herstatt, and Gemünden, 2006; Lüthje et al., 2005). The aforementioned findings should be regarded as prerequisites for the participation in a crowdfunding campaign; if people are not familiar or well informed with the product or service, the possibility of participating in its fundraising is low.

Literature has shown that the motivational factors can be aggregated into four major categories: *monetary rewards* (Harris, 2010; Horton & Chilton, 2010; Poetz & Schreiner, 2012), *social rewards* (Huberman, Romero & Wu, 2008), *psychological rewards* (Chinman, Aderson, Imm, Wandersman & Goodman, 1996; Van Sylke & Brooks, 2005;) or a *hybridization* of the former (Chanal & Caron-Fasan, 2008; Holley, 2010; Leimeister, Huber, Bretschneider & Krcmar, 2009; Mason & Watts, 2010; Schenk & Guittard, 2011).

Among the aforementioned motivational factors the monetary incentive could be conceived easy to be employed in crowd-funding method and especially in equity-based Crowd-funding. Yet the most successful crowd-funding campaigns were for projects (e.g. Luna Tik and Diaspora) that instead of giving shares or money they gave perks. This justifies the findings of studies that support the notion that the most successful crowdfunding campaigns are those that utilizes not only the monetary compensation, but also provides to participators the ability to take part in a project that offers the sense of community and provides enjoyment.

The marketing prism of Crowd-funding

In the Business domain, ventures that mostly use the crowd-funding method in order to get funds are from small to medium enterprises (SME) in their first steps of their development/operations. Hills (1995) noted that *“It was widely assumed in academia, even five years ago [about 1990], that Small and Medium Enterprises (SMEs) required just a simplified version of the more “sophisticated” marketing practices used by the largest companies. Now it is becoming apparent that marketing in SMEs is fundamentally different and more successful in SMEs than in large firms.”* Also, when an Enterprise is in its first steps of development, Kotler (2003:4-5) suggests that Entrepreneurial marketing concepts fit better to its practices. From the aforementioned assertions becomes apparent that the “less sophisticated” marketing practice that it is appropriate for a Start-Up Enterprise is what Kotler suggests as Entrepreneurial Marketing.

Kraus et al. (2009) defines Entrepreneurial Marketing as *“an organizational function and a set of processes for creating, communicating and delivering value to customers and for managing customer relationships in ways that benefit the organization and its stakeholders, and that is characterized by innovativeness, risk-taking, proactiveness, and may be performed without resources currently controlled”* (Keefe, 2004, p. 17). Entrepreneurial Marketing also is a field in academia that has been researched in depth; in the domain of Entrepreneurial Marketing has been proposed a different approach of marketing mix in order to meet the specific needs of a start-up Enterprise. The 4Ps that has been proposed by Zontanos and Anderson (2004) consists of Purpose Practice, Process and Person and sets four new variables through

which entrepreneurship can be expressed. Those variables are so fundamental for a Start-Up Enterprise that also can benefit the Crowd-funding campaign if it is utilized by the Start-Up Enterprise.

Conclusions and Implementation

With the advent of crowdfunding, consumers can now co-invest the production of a product or service. The ability to co-invest in the production of a “good” also transforms the marketing concept into a more genuine and “democratic” one; consumers can now decide which goods add value to them before even they be produced. Possibly it is time for Marketing Concept to be updated in order to better understand and express the new consumers’ norms so to be more effective in the market. Nowadays Marketing techniques also be applied by the customers and at the same time investors of the brand through crowd-funding and social media platforms by creating contents.

Moreover, crowdfunding has democratized the way a new business gets capital; consumers in the role of the investor are a healthier source of funds. The Market gets a broader meaning and encompasses consumers in the position of true power that can influence the business practice and promote products of true value. Yet entrepreneurs are not familiar with the concept of crowd-funding in order to utilize it so to get the aforementioned advances and at the same time consumers are not well familiarized with crowd-funding platforms.

It could help an entrepreneur and also a crowd-funding platform to understand how consumers’ investment decisions are influenced in the case of a crowdfunding campaign. This paper attempts to help understanding the method and its implementation by addressing the following research questions and also by creating a crowd-funding participation model.

- Could crowd-funding method be incorporated to all entrepreneurial ventures?
- Are there any benefits for the production of commodities and the delivering of services and if so, for what kind of products and services?

From reviewing the literature it is clear that people can be influenced by the industry and the product category in order to participate in crowdsourcing (Poetz and Schreier, 2012); with the same analogies in participation, a crowd-funding campaign can be influenced from those factors too. Also Crowd-funding is an innovative method and it is easier to attract consumers that are more willing to contribute in an innovative product or service. Furthermore it is easy understood that a product designed for a small group of people will find difficulties in the incorporation of Crowd-funding in order to fundraise money, as the core of Crowd-funding is in the crowd with a broader meaning. Finally but no least people will be discouraged to participate if they are not well informed

for the product or service (Baldwin et al., 2006; Lettl, Herstatt, and Gemünden, 2006; Lüthje et al., 2005); there are some products for example professional softwares that the vast majority of people are not familiar with. Crowd-funding could be incorporated with difficulties in entrepreneurial ventures unless the idea is an innovative and of a mass acceptance one.

- Does the classic Marketing concept benefit a crowd-funding strategy?

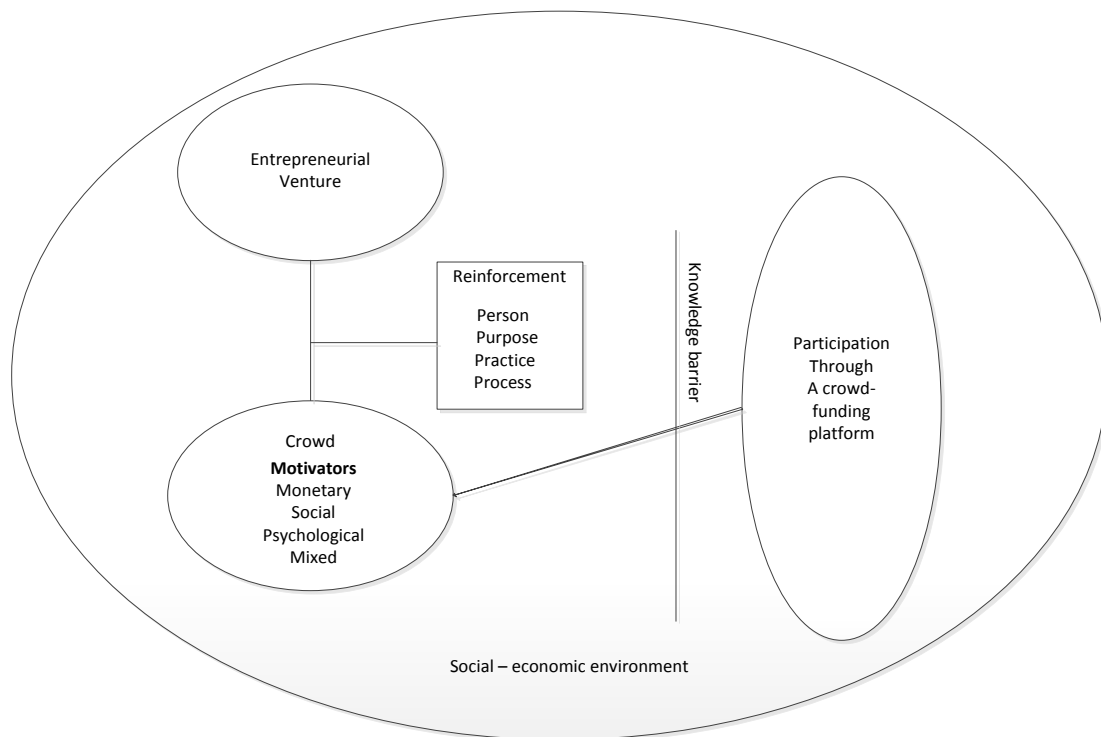
Marketing is fundamentally important in every product or service, yet a diversification in the marketing discipline, as an Entrepreneurial one, could provide a more effective mindset and tool in order to understand and influence the crowd. In the case of crowd-funding, which uses the model of Social media application in order to pool money for a start-up enterprise, it is apparent that the marketing implementation has to be more flexible, innovative and to work in a nonlinear environment. On the top of that an appropriate marketing approach for crowdfunding should have tools that handle in the best way network aspects.

By reviewing the literature it is concluded that the Entrepreneurial marketing is the best marketing approach for crowdfunding. The Entrepreneurial marketing is the interface of marketing and entrepreneurship; it encompasses all the aforementioned aspects, it is more flexible, it works in a nonlinear environment and takes seriously network and relationship aspects. Hills and Hultman (2006) in their study about the Entrepreneurial Marketing states that Entrepreneurial Marketing have a strong correlation with findings on the field of relationship marketing and network theory. In crowdfunding the way entrepreneurs influence their network and people that related to them is crucial and maybe the most important factor for their success.

Along with the network theories, the Marketing Mix that proposed by Zontanos and Anderson (2004), which includes the variables of Person, Process, Purpose and Practices, is not only a better frame for understanding marketing in the entrepreneurial firm but also important for the crowd-funding when it is utilized by the firm.

Another key factor for the creation of a crowdfunding participation model is the finding of the literature review that If knowledge base- entry barriers are high people will be discouraged to participate (Baldwin et al., 2006; Lettl, Herstatt, and Gemünden, 2006; Lüthje et al., 2005),

Participation model



Using the Practices, Purpose, Person and Process marketing mix, entrepreneurs can focus better on the network aspect of crowdfunding in order to leverage networks and to develop new market segments.

Practices: Decisions about which practices to follow should base on innovative thinking and making good use of resources.

Purpose: Asks to the answer what need does the firm fulfill, a fundamental question of each venture.

Person: Decisions based on the personal traits of the entrepreneur; acknowledge the personal traits could leads to a better strategical choices. Also the networks is a personal asset.

Process: The processes that the venture will develop, for example the process of developing of a new segment.

The 4P's triggers the motivators that lead the participation in a crowd-funding fundraising campaign; the motivators that are found in the literature review are: monetary, social, psychological and a mixed of the aforementioned.

Attention must be given in a project that the knowledge barriers are high; the project must be communicated with much of its details and a well written business plan in the facility of every prospect investor.

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