Crowd funding for financial inclusion. *"Giving Has Never Made Someone Poor."*

Vinod V. Nandaragi
Assistant Professor
B.V.V.Sangha's
Basaveshwara Degree College
Bidadi, Ramanagara, Karnataka, India
Email: vinnu.nandargi.696@gmail.com

Abstract:

The process of obtaining money by combining the efforts of several individual investors is known as crowd fundraising. The majority of crowd financing takes place online through websites and social media. Therefore, crowd financing is the process of obtaining modest sums of money from a large number of individuals, primarily through the Internet or specialized websites, in order to finance a project or business. Fund raising for entrepreneurial endeavors, including companies and artistic and creative enterprises, has also been arranged through crowd fund raising. Crowd fundraising is estimated to have raised around US$34 billion globally in 2015. You've probably heard several stories of a guy or woman using the internet to raise millions of dollars for her father's or other family members' medical care. Actually, crowd financing is used to accomplish this gathering. An 11-year-old girl in Hyderabad has raised Rs. 6.2 lacs using crowdsourcing or community finance to help feed a large number of impoverished individuals who lost their jobs as a result of the nation's COVID-19 outbreak. You must now have a fundamental understanding of crowd funding's purpose and goals.

The key takeaways from this case can be summarized as follows. There is no doubt that entering the world of crowd funding is challenging and takes time, determination and a specific skill set. In the words of this entrepreneur "there are so many unknowns". According to Simon, crowd funding involves a huge "learning curve" and requires "considerable time, skills and commitment. It takes considerable time to build trust between backers, developing a good image of the product, promotional skills and to understand details of costs and components and manufacturing and the logistics process".

Key Words: Crowd Funding, Financial Inclusion, Digital Finance.

Introduction:

Crowd funding is the practice of funding a project or venture by raising money from a large number of people, in modern times typically via the Internet. Crowd funding is a form of crowd sourcing and alternative finance. In the new digital economy, crowd funding has emerged as a powerful and disruptive tool transforming the financial landscape for entrepreneurs worldwide. Across numerous continents and sectors as diverse as information technology, creative arts, social and community groups, have effusively embraced this new funding source.

Crowd funding is a term that has become a powerful yet disruptive force for entrepreneurs worldwide in accessing start-up funding. Typically, it involves raising funding from the crowd often referred to as backers. Money can be raised by a large number of individuals (so called backers) who each typically contribute a small amount, usually via the internet online to help entrepreneurs (and community projects) access much needed findings outside the traditional financial system.

Although similar concepts can also be executed through mail-order subscriptions, benefit events, and other methods, the term crowd funding refers to Internet-mediated registries. This modern crowd funding model is generally based on three types of actors - the project initiator who proposes the idea or project to be funded, individuals or groups who support the idea, and a moderating organization (the "platform") that brings the parties together to launch the idea.

Given the number of crowd funding platforms, one of the first challenges facing a start-up moving into the crowd funding arena is to identify the most suitable platform for their product or company (Dushnitsky and Fitza, 2018). According to Brown et al. (2018), communications between funders and the crowds make crowd funding much more complicated and time consuming than alternatives. Moreover, entrepreneurs need to find the right crowd funding platform for their types of businesses and adopt crowd funding as a planned financial method.

Crowd funding on the internet first gained popular and mainstream use in the arts and music communities. The first noteworthy instance of online crowd funding in the music industry was in 1997, when fans of the British rock band Marillion raised US$60,000 in donations by means of an Internet campaign to underwrite an entire U.S. tour. The band subsequently used this method to fund their studio albums.

Review of Literature:

As research into crowd funding has developed, an area that has been the subject of recent debate is the link between crowd funding and the development of high-technology innovative start-ups. As far back as Schumpter (1912) innovation and new business development have been linked with economic output and growth (Holmberg, 2016). Recently, Audretsch et al. (2020) argue that innovative and high technology start-ups create new industries and considerable economic and societal impact.

As noted by Herve and Schwienbacher (2018), it is in this area that crowd funding offers significant gains. Typically, new technology start-up businesses tend to be considered risky, making traditional sources of finance a major challenge. Moreover, because these firms can be relatively small, without a trading history, they face with additional problem of significant asymmetry information problems (Carpenter and Peterson, 2002; King and Levine 1993).

This has led to a growing body of research which has examined crowd funding from a supply side. Research has examined the dynamics and motivations among investors to participate in crowd funding activities

(Kuppuswamy and Bayus, 2018). Studies have identified a range of motivations that drive investors including financial returns (Shafi, 2019); participating in innovative projects (Burger and Kleinert, 2020); advancing personal growth (Wald, et al., 2019); being part of a like-minded community (Belleflamme et al., 2014; Kim and Petrick, 2020; Lukkarinen et al., 2016).

Working of Crowd Funding:

- The entrepreneur who wants to raise funds through crowd funding and the small investors who are interested in funding new businesses and business ideas needs to register at the official crowd funding websites. These websites are the medium between investors and entrepreneurs.
- The entrepreneur has to put the idea along with projections of the business through the crowd funding website so that the potential investors could decide whether to invest or not to invest.
- Along with the idea and projections, the entrepreneur has to quote the minimum amount the investor can invest. The minimum amount can be as low as $10.
- The potential investor needs to show interest in investing along with the minimum amount it can invest and the procedure as well as details of the investments.
- If over applications are received, the excess money is to be repaid to the investors.
- Once the funds are raised and received, the entrepreneur has to pay fees to the crowd funding websites. The fee is based on the percentage of fundraising.
- The percentage of profit generated from the business needs to be shared with the investors by way of return on investment.

Rules for Crowd Funding:

- All the Transactions from the fund raised from crowd funding needs to be registered with the security exchange commission unless it meets the exemption criteria defined by the commission.
- Projects are needed to be displayed at the website as well as they are to be registered with the security exchange commission and the business for which funds are to be raised needs to be legal.
- Transparent accounts and movement of fund statement is to be displayed at the website so that the investors can get the information about the application of their funds.
- Security Exchange Commission needs to put the yearly limit on the amount to be raised in aggregate as well as individual investor wise.

Challenges of Crowd Funding:

Accessing funding is a universal problem for entrepreneurs. Starting a business and securing funding is a major challenge for entrepreneurs throughout the world. This is particularly the case in rural regions and less developed countries.

- All disclosures and information need to be filed with the security exchange commission.
  - Attracting potential investors is a difficult task as the company needs to earn trust through convincing projects.
  - More transparency and registration of transactions with the security exchange commission may lead to no secrecy as the business needs secrecy regarding some important matters.
  - The targets and deadlines defined in the project need to be fulfilled on time and should be realistic in nature.
  - Timely returns are the biggest challenge as because of low or no returns, the ratings, and the reputation of the organization are affected.

Risks Involved in Crowd Funding:

- The major risk involved in crowd funding is the risk of fraud or loss of investment.
- The risk of a company might not fulfill the commitments at the time due to unfavorable business conditions or any other reasons.
- Risk of failure of the projected plan and dealing with it.
- Risk of payment of a return on investment on a timely basis.

The challenge of accessing funding as a start-up

Accessing funding is a universal problem for entrepreneurs. Starting a business and securing funding is a major challenge for entrepreneurs throughout the world. This is particularly the case in rural regions and less developed countries such as Africa and Asia (Chae et al 2020) with less developed financial markets. In addition, securing funding for innovative ideas has been identified as problematic resulting in a funding gap for innovative start-ups

In the context of Ireland, despite having a really dynamic and supportive entrepreneurial culture, accessing funding is still a major challenge for several reasons. Firstly, the funding sector for business in Ireland is problematic largely due to the fact that the three main banks - BoI, AIB and Ulster Bank – have a triopoly on lending to the SME sector. The latter control some 95% of SME funding. Secondly, research from the Central Bank of Ireland Report (2018) indicates that Irish SMEs are about 50 percent less likely to apply for bank funding than their EU counterparts, and that bank rejection rates for SME loans is more than twice the rate in comparator EU countries. While enterprise support agencies, venture capitalist (VCs) and business angel markets have increasingly played an important part, this is not without its challenges (Hellman, 1998). VCs can often seek high levels of ownership and control of the business, with an expectation of a high rate of return. Within the last ten years, access to funding has certainly improved, but there are still major obstacles for many start-up or early stage businesses. For example, in terms of crowd funding, research by the Department of Finance 2018 acknowledged that the crowd funding market in Ireland was relatively small accounting for less than 0.4 percent of the SME finance market. The comparable figure for the UK was 12 percent. The report also recognizes the potential of crowd funding for Irish entrepreneurs is not fully exploited due to a lack of information among SME and entrepreneurs in the value of non-banking finance.

Protection from Cybercrimes

Crowd funding Platform/Website is the center point of interaction between the companies and the prospective investors. Moreover, it will also function as the repository of all the information and disclosures provided by the companies periodically. It occupies a very crucial position in the entire infrastructure. Therefore, it needs to be secure and safe from all types of cyber-attacks. To protect the Crowd funding platform from hacking/identity theft, etc., the necessary steps need to be taken by the owners of the Crowd funding Platform. To provide communication security over the Internet, the crowd funding platforms should be layered over Transport Layer Security (TLS)/ Secure Sockets Layer (SSL). Platform owner should ensure safety, secrecy, integrity and retrievability of the data. The platform owner shall have a adequate back-up, and Disaster management and recovery and restoration plans. It is desirable that platform owners draft a security policy which shall, then, be put in public for comments and analysis. There shall be regular audits by reputed external auditors who is CISA (Certified Information Systems Auditor) or otherwise appropriately qualified that the security measures taken by the Platform Owners are adequate and meet the requirements and that risk management systems are in place to identify and mitigate the risks arising out of the regular operations.

Crowd funding in India

Crowd funding is a concept that has existed for a while in western countries and is relatively new in India. Crowd funding is a means to raise a smaller amount of funds from a larger number of peoples mainly via the internet. In this article, we look at the basics of crowd funding and its growth in India. Crowd funding is a manner of raising funds for a project or a venture through internet by raising capital from a large number of individual investors. Crowd funding is mostly done online via social media and websites. In the present times, crowd funding has been used widely for arranging funds for the entrepreneurial ventures such as artistic projects, startups, medical expenses, travel and community oriented social entrepreneurship projects etc.

Ketto, an Indian crowd funding platform, raised over Rs 115 crore through its campaigns related to Covid-19 and registered a 4X growth during the lockdown. ImpactGruru, another such platform, saw donations double per minute post COVID averaging 2.5 donations per minute now. Faircent, a P2P lending platform, disbursed loans worth Rs 1,150 crore between April to March20-21. The success of these crowd funding platforms proves that calamities indeed bring humans together. And, that the pandemic was no different. In fact, the PM Cares Fund, set up by the Prime Minister of India to channelise philanthropic contributions towards the fight against corona, also used the crowd funding mechanism. It also proves that such platforms, if used in the right manner, can help innumerable people access aid.

"For the first time in eight years, Ketto has seen a surge in first-time donors across Tier II and Tier III cities. We recorded a 300 per cent increase in first-time donors in the last one year," said Varun Sheth, Founder and CEO, Ketto. Apart from scores of campaigns for medical emergencies, Ketto supported several fundraisers for small entrepreneurs and SMEs. One such SME was The House of Artisans, which makes handmade products and employs about 200 rural artisans. For the second year in a row, finance minister Nirmala Sitharaman prioritized growth above fiscal reduction, dramatically increasing investment and spending on infrastructure in the Union Budget for the fiscal year beginning April 1, 2022 While calling for fragmented urban development in Tier 2 and 3 cities, the budget recognizes the significance of going beyond 'business as usual' and 'reimagining cities. This has opened the door for numerous new generation.

Is Crowd funding really needed?

In the earlier, the 2008 financial crisis resulted in failure of number of Banks and, consequently, the new capital adequacy regulations for banks, such as Basel III were implemented. As a result, credit providers have become increasingly constrained in their ability to lend money to the real economy. IOSCO Paper states that the amount of bank loans made in Western Europe and the USA dropped significantly at the beginning of the crisis. While there have been some signs of recovery in the US (although the growth rate is still below pre-crisis levels), in Western Europe the growth rate in loans to the non-financial corporate sector has been negative, especially to SMEs in the EU. In this funding vacuum, peer-to-peer lending and other Crowdfunding Platforms are growing in popularity, as bank liquidity is reduced and new regulatory requirements make obtaining loans for small and medium enterprises and individuals difficult.

In India, during the last few years, the IPO market has not been very active. Though, SEBI, has been at the forefront in facilitating fund raising by SMEs through measures like SME segment in Stock Exchanges, Category I- SME funds under AIF, Institutional Trading Platform, etc., still there is need to encourage innovative way of fund raising to provide an impetus to genuine SMEs/Start-ups and to explore other alternative models of fund raising with appropriate framework in consonance with retail investor protection. Since the "Crowd funding" phenomenon is gaining its popularity, its importance cannot be ignored. To regulate crowd funding, it is very important to take note that while it is necessary to ensure that Start-ups/SMEs could raise funds at ease, it is equally important to ensure that no systemic risks are created wherein retail investors are lured by some unscrupulous players by substituting the existing framework, which has been developed over a period of time through experience and observation. Hence, there is Page 28 of 66 necessity to strike a proper balance between investor protection and the role equity markets can play in supporting economic development and growth. 8.5 While some regulators are criticized by media from "taking the crowd out of crowdfunding',8 there are also media reports explaining the risks in the model and stating that regulators who are today denounced for their intervention will then be castigated for their neglect.9

Crowd funding vs Private Equity

In crowd funding, the entrepreneur gets a single platform to showcase a business idea or business, share the pitch to a large online audience and generate funds either through pre-order of products or through sale of items at a discount. Crowd funding makes it easier for an entrepreneur to reach a wide range of audience interested in contributing small amounts of funding mostly in return for goods or services.

To obtain private equity, on the other hand, the Entrepreneur must showcase his/her business idea to a limited set of investors or High Net Worth Individuals (HNIs), in the hopes of having one of them invest in the business in return for equity. One of the major difference between crowd funding and private equity is that in private equity, the Entrepreneur must provide equity in return for capital. On the other hand, crowd funding doesn't require the Entrepreneur to give up any equity thereby being a much more attractive option for innovative startups and startups with huge growth potential. Also, crowd funding in most cases serves as seed fund to get the business started. Whereas, private equity is usually provided after the business has generated certain tractions.

Crowd funding vs Bank Loan

Crowd funding and bank loan are again very different forms of financing. Bank loan usually requires repayment and collateral security, whereas crowd funding doesn't need either. Also, with crowd funding, even a business that has no track record or an innovative business model can get funded. Bank loan mostly requires a proven track record and/or proven business model for financing.

Crowd funding advantages

Crowd funding has numerous advantages when compared to private equity or bank loan as follows:

1. Entrepreneurs have the freedom to innovate naturally in a domain of their choice.
2. Crowd funding can be done successfully if the promoters have a good social media presence and a well large network of friends.
3. No requirement to give up any equity.
4. No requirement to have a repayment plan and/or interest payments.
5. Ability to attract a wide range of investors.
6. Also, serves as a marketing channel.
7. No minimum fundraise requirement.
8. Progress of a funding campaign can be easily tracked only.

Conclusion

Crowd funding is a phenomenon which is characterized with high dynamics. It promotes and represents new innovations and validates the market demands through investments by the investors. Through the process of crowd funding a new product development life cycle is developed and promoted. Therefore, it can be concluded that the crowd funding potentially accelerates the innovations and new ideas.

Crowd funding, the term itself have an inexorably noteworthy criticalness it makes a baby youth industry develop quick and additionally gives new interest avenues and gives something else to portfolio update of analysts. It is the new point of view for the vigorous people to fire up a business. The goal of this study has been centered on its issues and difficulties, its insistence in Indian condition, and hazard related with the business itself. The appraisal itself is undeniable in nature. The associate information's have been amassed from different research studies, websites, magazines & journals etc.

References

1. Agrawal, A., Catalini, C. and Goldfarb, A. (2015), "Crowdfunding: geography, social networks, and the timing of investment decision". *Journal of Economics & Management Strategy,* 24, No. 2, pp. 253-274. https://doi.org/10.1111/jems.12093
2. Appio, F. P., Leone, D., Platania, F. and Schiavone, F. (2020), "Why are rewards not delivered on time in rewards-based crowdfunding campaigns? An empirical exploration", *Technological Forecasting and Social Change*, Vol. 157, pp. 1-9. https://doi.org/10.1016/j.techfore.2020.120069
3. Audretsch, D., Colombelli, A., Grilli, L., Minola, T. and Rasmussen, E. (2020). "Innovative start-ups and policy initiatives", *Research Policy*, Vol. 49, No. 10, pp. 1-14. https://doi.org/10.1016/j.respol.2020.104027
4. Bapna, S. (2017), "Complementarity of Signals in Early-Stage Equity Investment Decisions: Evidence from a Randomized Field Experiment", *Management Science*, Vol. 65, No. 2, pp. 459-954. https://doi.org/10.1287/mnsc.2017.2833
5. Belleflamme, P., Lambert, T. and Schwienbacher, A. (2014). "Crowdfunding: Tapping The Right Crowd", *Journal of Business Venturing*, Vol. 29, No. 5, pp. 585-609. https://doi.org/10.1016/j.jbusvent.2013.07.003
6. Bollaert, H., Leboeuf, G. and Schwienbacher, A. (2020), "The narcissism of crowd funding entrepreneurs", *Small Business Economics*, Vol. 55, pp. 57-76. . https://doi.org/10.1007/s11187-019-00145-w
7. Brown, R., Mawson, S. and Rowe, A. (2019), "Start-ups, entrepreneurial networks and equity crowdfunding: A processual perspective", *Industrial Marketing Management*, Vol. 80, pp. 115-125. https://doi.org/10.1016/j.indmarman.2018.02.003
8. Brown, R., Mawson, S., Rowe, A. and Mason, C. (2018), "Working the crowd: Improvisational entrepreneurship and equity crowd funding in nascent entrepreneurial ventures", *International Small Business Journal*, Vol. 36, No. 2, pp. 169-193. https://doi.org/10.1177%2F0266242617729743
9. Bruton, G., Khavul, S., Siegel, D. and Wright, M. (2015), "New Financial Alternatives in Seeding Entrepreneurship: Microfinance, Crowd funding, and Peer–to–Peer Innovations", *Entrepreneurship Theory and Practice*, Vol. 39, No. 1, pp. 9-26. https://doi.org/10.1111%2Fetap.12143

10. Burtch G., Ghose A. and Wattal S. (2013), “An empirical examination of the antecedents and consequences of contribution patterns in crowd-funded markets”, *Information System Research*, Vol. 24, No. 3, pp. 449-519. https://doi.org/10.1287/isre.1120.0468
11. Bürger, T. and Kleinert, S. (2020). "Crowdfunding cultural and commercial entrepreneurs”, *Small Business Economics*, https://doi.org/10.1007/s11187-020-00419-8
12. Central Bank of Ireland (2018), *SME Market Report 2018*, [Online] Available at: https://www.centralbank.ie/docs/default-source/publications/sme-market-reports/sme-market-report-2018.pdf?sfvrsn=6 (access on 15 December 2020).
13. Chao, E. J., Serwaah, P., Baah-Peprah, P. and Shneor, R. (2020), "Crowdfunding in Africa: Opportunities and Challenges", In: Shneor R., Zhao L., Flåten BT. (eds) *Advances in Crowdfunding*. Cham: Palgrave Macmillan, pp. 319-339. https://doi.org/10.1007/978-3-030-46309-0_14
14. Colombo, M. G. and Grilli, L. (2007), "Funding gaps? Access to bank loans by high-tech start-ups", *Small Business Economics*, Vol. 29, pp. 25-46. https://doi.org/10.1007/s11187-005-4067-0
15. Cowden, B. J. and Young, S. L. (2020), "The copycat conundrum: The double-edged sword of crowd funding", *Business Horizons*, Vol. 63, No. 4, pp. 541-551. https://doi.org/10.1016/j.bushor.2020.03.012